

GARETH R. JONES JENNIFER M. GEORGE

ESSENTIALS OF

contemporary management




SECOND edition

ASHFORD
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Essentials of
**Contemporary
Management**

Second Edition

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Essentials of Contemporary Management

Second Edition

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ASHFORD
UNIVERSITYSM
FOUNDED 1918



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Brief Contents

PART ONE

Management and Managers	1
-------------------------	---

CHAPTER ONE

The Management Process Today	2
------------------------------	---

Appendix: History of Management Thought	41
---	----

CHAPTER TWO

Values, Attitudes, Emotions, and Culture: The Manager as a Person	50
---	----

PART TWO

The Environment of Management	87
-------------------------------	----

CHAPTER THREE

Managing Ethics and Diversity	88
-------------------------------	----

CHAPTER FOUR

Managing in the Environment	136
-----------------------------	-----

PART THREE

Planning, Decision Making, and Competitive Advantage	169
--	-----

CHAPTER FIVE

Decision Making, Learning, Creativity, and Innovation	170
---	-----

CHAPTER SIX

Planning, Strategy, and Competitive Advantage	200
---	-----

PART FOUR

Organizing and Change	239
-----------------------	-----

CHAPTER SEVEN

Designing Organizational Structure	240
------------------------------------	-----

CHAPTER EIGHT

Control, Change, and Entrepreneurship	282
---------------------------------------	-----

PART FIVE

Leading Individuals and Groups	319
--------------------------------	-----

CHAPTER NINE

Motivation	320
------------	-----

CHAPTER TEN

Leaders and Leadership	354
------------------------	-----

CHAPTER ELEVEN

Effective Team Management	386
---------------------------	-----

CHAPTER TWELVE

Building and Managing Human Resources	418
---------------------------------------	-----

PART SIX

Controlling Essential Activities and Processes	453
--	-----

CHAPTER THIRTEEN

Communication and Information Technology Management	454
---	-----

CHAPTER FOURTEEN

Operations Management: Managing Vital Operations and Processes	488
--	-----

Appendix B: Career Development	513
--------------------------------	-----

VIDEO CASES

GLOSSARY

NOTES

PHOTO CREDITS

NAME INDEX

SUBJECT INDEX

COMPANY INDEX

Contents

Chapter One

The Management Process Today

2



Management Snapshot
Different Approaches to
Management at the Home
Depot and Lowe's:
What Is High-Performance
Management? 3

Overview

What Is Management?	5	IT and Managerial Roles and Skills	19
Achieving High Performance:		Managerial Roles Identified by Mintzberg	19
A Manager's Goal	5	Being a Manager	23
Why Study Management?	6	Managerial Skills	23
Managerial Functions	7	Challenges for Management in a Global Environment	27
Planning	8	Building Competitive Advantage	28
Organizing	11	Maintaining Ethical and Socially Responsible Standards	30
Leading	12	Managing a Diverse Workforce	31
Controlling	12	Utilizing IT and E-Commerce	33
Types of Managers	13		
Levels of Management	13		
Areas of Managers	15		
Recent Changes in Managerial Hierarchies	16		

Chapter Two

Values, Attitudes, Emotions, and Culture: The Manager as a Person

50



Management Snapshot
Employees Come First at
PAETEC 51

Overview

Enduring Characteristics		Organizational Culture	71
Personality Traits	52	Managers and Organizational Culture	71
The Big Five Personality Traits	53	The Role of Values and Norms in Organizational Culture	73
Other Personality Traits That Affect Managerial Behavior	58	Culture and Managerial Action	78
Values, Attitudes, and Moods and Emotions	60		
Values: Terminal and Instrumental	60		
Attitudes	62		
Moods and Emotions	67		
Emotional Intelligence	68		

Examples

Manager as a Person

New CEOs Bring Change at Avon and Lucent 10

Information Technology Byte

Empire Insurance Uses CRM to Boost Sales 18

Manager as a Person

Steve Jobs Transforms Apple Computer 25

Ethics in Action

Diet Supplement Makers and the FDA 30

Focus on Diversity

How Diversity Can Promote Competitive Advantage 31

Management in Action

Summary and Review 33

Management in Action 35

Topics for Discussion and Action 35

Building Management Skills:

Thinking About Managers and

Management 35

Small Group Breakout Exercise:

Opening a New Restaurant 36

Be the Manager 36

Additional Activities on the Build

Your Management Skills DVD 37

Managing Ethically 37

BusinessWeek Case in the News:

The Hard Work in Leadership 37

BusinessWeek Case in the News:

Can a U.S.-Style Boss Rev Up

Siemens? 39

Appendix: History of Management Thought 41

F.W. Taylor and Scientific Management 41

Weber's Bureaucratic Theory 43

The Work of Mary Parker Follett 45

The Hawthorne Studies and

Human Relations 46

Theory X and Theory Y. 47

Examples

Information Technology Byte

Sam Palmisano Reinvents IBM 56

Ethics in Action

Taking Responsibility for Exposing Wrongdoing 58

Ethics in Action

The Courage to Be Honest 62

Focus on Diversity

Changing Attitudes 63

Manager as a Person

Bernie Goldhirsh's Legacy 69

Management in Action

Summary and Review 80

Management in Action 81

Topics for Discussion and Action 81

Building Management Skills:

Diagnosing Culture 81

Small Group Breakout Exercise:

Making Difficult Decisions in

Hard Times 82

Be the Manager 83

Additional Activities on the Build

Your Management Skills DVD 83

Managing Ethically 83

BusinessWeek Case in the News: The Wizard Of Odd 83

BusinessWeek Case in the News:

The Immelt Revolution 85

Contents

Chapter Three

Managing Ethics and Diversity

88



Management Snapshot

How to Strengthen an Organization's Code of Ethics 89

Overview

The Nature of Ethics	91	Sources of an Organization's Code of Ethics	104
Ethical Dilemmas	91	Ethical Organizational Cultures	106
Ethics and the Law	91		
Changes in Ethics over Time	92	The Increasing Diversity of the Workforce and the Environment	109
Stakeholders and Ethics	94	Age	110
Stockholders	94	Gender	110
Managers	95	Race and Ethnicity	112
Employees	96	Religion	114
Suppliers and Distributors	97	Capabilities/Disabilities	114
Customers	97	Socioeconomic Background	116
Community, Society, and Nation	97	Sexual Orientation	117
Rules for Ethical Decision Making	99	Other Kinds of Diversity	118
Why Should Managers Behave Ethically?	102		

Chapter Four

Managing in the Environment

136



Management Snapshot

Korea's LG (Lucky Goldstar) Wants to Be the New Leader in Global Electronics 137

Overview

What Is the Organizational Environment?	138	The General Environment	148
The Task Environment	140	Economic Forces	149
Suppliers	140	Technological Forces	149
Distributors	143	Sociocultural Forces	150
Customers	144	Demographic Forces	151
Competitors	146	Political and Legal Forces	152
		Global Forces	154

	Examples	Management in Action
Managers and the Effective Management of Diversity 119	Ethics in Action	Summary and Review 126
Critical Managerial Roles 119	Johnson & Johnson's Ethical Culture 108	Management in Action 127
Effectively Managing Diversity Makes Good Business Sense 121	Managing Globally	Topics for Discussion and Action 127
Sexual Harassment 124	Asians and Hispanics Projected to Be Fastest-Growing Group 112	Building Management Skills: Solving Diversity-Related Problems 127
Forms of Sexual Harassment 124	Focus on Diversity	Small Group Breakout Exercise: Determining If a Problem Exists 127
Steps Managers Can Take to Eradicate Sexual Harassment 125	Gays and Lesbians in the Workplace 117	Be the Manager 128
	Manager as a Person	Additional Activities on the Build Your Management Skills DVD 128
	Creating a Business Through Sheer Determination 121	Managing Ethically 128
		BusinessWeek Case in the News: AIG: What Went Wrong 129
		BusinessWeek Case in the News: Hispanic Nation 131

	Examples	Management in Action
The Changing Global Environment 154	Managing Globally:	Summary and Review 164
Declining Barriers to Trade and Investment 155	Global Supply Chain Management 142	Management in Action 165
Declining Barriers of Distance and Culture 156	Information Technology Byte:	Topics for Discussion and Action 165
Effects of Free Trade on Managers 159	Designing Global Information Systems 145	Building Management Skills: Analyzing an Organization's Task and General Environments 165
The Role of National Culture 160	Managing Globally:	Small Group Breakout Exercise: How to Enter the Copying Business 166
Hofstede's Model of National Culture 161	American Rice Invades Japan 147	Be the Manager: The Changing Environment of Retailing 166
National Culture and Global Management 163	Managing Globally:	Additional Activities on the Build Your Management Skills DVD 166
	Car Manufacturing Is Changing Around the World 153	Managing Ethically 167
	Managing Globally:	BusinessWeek Case in the News: The Vanishing Mass Market 167
	E-Commerce and Global Customer Responsiveness 157	BusinessWeek Case in the News: Posco: One Sharp Steelmaker 168

Contents

Chapter Five

Decision Making, Learning, Creativity, and Innovation

170



Management Snapshot
Revising Decisions and
Plans Never Ends for Craig
Knouf 171

Overview

The Nature of Managerial Decision Making	172	Generate Alternatives	181
Programmed and Nonprogrammed Decision Making	173	Evaluate Alternatives	182
The Classical Model	176	Choose Among Alternatives	184
The Administrative Model	177	Implement the Chosen Alternative	185
Steps in the Decision-Making Process	179	Learn from Feedback	185
Recognize the Need for a Decision	180	Group Decision Making	185
		The Perils of Groupthink	187
		Devil's Advocacy	188
		Diversity Among Decision Makers	188

Chapter Six

Planning, Strategy, and Competitive Advantage

200



Management Snapshot
Chris McCormick's New
Strategy for L.L. Bean 201

Overview

The Nature of the Planning Process	202	Formulating Strategy	212
Levels of Planning	203	SWOT Analysis	213
Who Plans?	206	The Five Forces Model	216
Time Horizons of Plans	206	Formulating Corporate-Level Strategies	217
Standing Plans and Single-Use Plans	207	Concentration on a Single Business	217
Why Planning Is Important	207	Diversification	218
Scenario Planning	208	International Expansion	219
Determining the Organization's Mission and Goals	209	Vertical Integration	225
Defining the Business	209		
Establishing Major Goals	211		

	Examples	Management in Action
Organizational Learning and Creativity		Summary and Review 194
Creating a Learning Organization	Manager as a Person Curbing Overconfidence 175	Management in Action 195
Promoting Individual Creativity	Ethics in Action NASA's Flawed Culture 183	Topics for Discussion and Action 195
Promoting Group Creativity	Information Technology Byte Improving Medical Decision Making 186	Building Management Skills: How Do You Make Decisions? 196
Promoting Creativity at the Global Level	Focus on Diversity Asking Different Questions and Providing Different Answers 190	Small Group Breakout Exercise: Brainstorming 196
		Be the Manager
		Additional Activities on the Build Your Management Skills DVD 196
		Managing Ethically 197
		Case for Discussion: Yamada Transforms GlaxoSmithKline 197
		BusinessWeek Case in the News: The Brains Behind BlackBerry 198

	Examples	Management in Action
Formulating Business-Level Strategies	Management Insight Ups and Downs at Mattel 210	Summary and Review 233
Low-Cost Strategy	Manager as a Person Douglas Conant Is in the Soup 214	Management in Action 235
Differentiation Strategy	Managing Globally Levi Strauss's Big Problems 222	Topics for Discussion and Action 235
"Stuck in the Middle"	Managing Globally Strategy in the World Package Delivery Business 228	Building Management Skills: How to Analyze a Company's Strategy 235
Focused Low-Cost and Focused Differentiation Strategies		Small Group Breakout Exercise: Low Cost or Differentiation? 236
Formulating Functional-Level Strategies		Be the Manager 236
Planning and Implementing Strategy		Additional Activities on the Build Your Management Skills DVD 236
		Managing Ethically 237
		BusinessWeek Case in the News: Volkswagen Slips Into Reverse 237
		BusinessWeek Case in the News: Imagine Sony on Steroids 238

Contents

Chapter Seven

Designing Organizational Structure

240



Management Snapshot
How Three CEOs Worked to
Reorganize Lucent 241

Overview

Designing Organizational
Structure 243

The Organizational
Environment 243
Strategy 244
Technology 245
Human Resources 247

Grouping Tasks into Jobs:
Job Design 248

Job Enlargement and Job
Enrichment 249
The Job Characteristics
Model 250

Grouping Jobs into
Functions and Divisions 251

Functional Structure 252
Divisional Structures: Product,
Market, and Geographic 254
Matrix and Product Team
Designs 260
Hybrid Structure 262

Chapter Eight

Control, Change, and Entrepreneurship

282



Management Snapshot
Control Is No Longer a
Problem for Oracle 283

Overview

What Is Organizational
Control? 285

The Importance of
Organizational Control 285
Control Systems and IT 287
The Control Process 288

Output Control 292

Financial Measures of
Performance 292
Organizational Goals 293
Operating Budgets 295
Problems with Output
Control 296

Behavior Control 298

Direct Supervision 298
Management by Objectives 299
Bureaucratic Control 300
Problems with Bureaucratic
Control 302

Organizational Culture
and Clan Control 303

Adaptive Cultures versus Inert
Cultures 305

	Examples	Management in Action
Coordinating Functions and Divisions		Summary and Review 275
Allocating Authority	264	Management in Action 277
Types of Integrating Mechanisms	269	Topics for Discussion and Action 277
Strategic Alliances, B2B Network Structures, and IT	272	Building Management Skills: Understanding Organizing 277
	Manager as a Person	Small Group Breakout Exercise: Bob's Appliances 278
	Wayne Inouye Has to Restructure Gateway 244	Be the Manager: Speeding Up Web-Site Design 278
	Management Insight	Additional Activities on the Build Your Management Skills DVD 279
	GlaxoSmithKline's New Product Structure 257	Managing Ethically 279
	Managing Globally	BusinessWeek Case in the News: No Excuse Not to Succeed 279
	Nokia, Dow, and the LEGO Company Revamp Their Global Structures to Raise Performance 259	BusinessWeek Case in the News: How Xerox Got Up to Speed 280
	Managing Globally	
	Plexus Uses Self-Managed Teams to Decentralize Authority 268	
	Ethics in Action	
	Of Shoes and Sweatshops 274	

	Examples	Management in Action
Organizational Change	307	Summary and Review 314
Assessing the Need for Change	308	Management in Action 315
Deciding on the Change to Make	309	Topics for Discussion and Action 315
Implementing the Change	310	Building Management Skills: Understanding Controlling 315
Evaluating the Change	310	Small Group Breakout Exercise: How Best to Control the Sales Force? 316
Entrepreneurship, Control, and Change	311	Be the Manager 316
	Managing Globally	Additional Activities on the Build Your Management Skills DVD 316
	Wal-Mart Uses Output Control to Expand Internationally 295	Managing Ethically 317
	Management Insight	BusinessWeek Case in the News: The "Constant Challenge" at eBay 317
	How to Kill Customer Satisfaction 301	BusinessWeek Case in the News: Vital Signs at Humana 318
	Manager as a Person	
	James Casey Creates a Culture for UPS 304	
	Management Insight	
	Entrepreneurship at Maden Technologies 312	

Contents

Chapter Nine

Motivation

320



Management Snapshot

Motivating Employees at the SAS Institute 321

Overview

The Nature of Motivation	322	Equity Theory	332
Expectancy Theory	324	Equity	332
Expectancy	325	Inequity	333
Instrumentality	327	Ways to Restore Equity	333
Valence	327	Goal-Setting Theory	335
Bringing It All Together	327	Learning Theories	338
Need Theories	329	Operant Conditioning Theory	338
Maslow's Hierarchy of Needs	329	Social Learning Theory	340
Herzberg's Motivator-Hygiene Theory	331	Pay and Motivation	342
McClelland's Needs for Achievement, Affiliation, and Power	331	Basing Merit Pay on Individual, Group, or Organizational Performance	342
Other Needs	332	Salary Increase or Bonus?	343
		Examples of Merit Pay Plans	344

Chapter Ten

Leaders and Leadership

354



Management Snapshot

John Mackey's Personal Leadership Style 355

Overview

The Nature of Leadership	357	The Leader Substitutes Model	369
Personal Leadership Style and Managerial Tasks	357	Bringing It All Together	370
Leadership Styles across Cultures	358	Transformational Leadership	371
Power: The Key to Leadership	358	Being a Charismatic Leader	372
Empowerment: An Ingredient in Modern Management	361	Stimulating Subordinates Intellectually	372
Trait and Behavior Models of Leadership	362	Engaging in Developmental Consideration	373
The Trait Model	362	The Distinction between Transformational and Transactional Leadership	373
The Behavior Model	363	Gender and Leadership	373
Contingency Models of Leadership	365	Emotional Intelligence and Leadership	376
Fiedler's Contingency Model	365		
House's Path-Goal Theory	367		

Examples

Information Technology Byte

Boosting Expectancy at Best Buy 326

Focus on Diversity

Nike's Efforts to Appeal to Diverse
Customers 328

Focus on Diversity

Dick Parsons Gets Time Warner
Back on Track 336

Management in Action

Summary and Review 345

Management in Action 347

Topics for Discussion and Action 347

Building Management Skills:

Diagnosing Motivation 347

Small Group Breakout Exercise:

Increasing Motivation 348

Be the Manager 348

Additional Activities on the Build

Your Management Skills DVD 349

Managing Ethically 349

Case for Discussion: Tindell and

Boone Inspire and Motivate at

the Container Store 349

BusinessWeek Case in the News:

Coverup at Boeing? 350

Examples

Managing Globally

Toyota Is on a Roll 363

Management Insight

Supporting Creativity 368

Focus on Diversity

Kathleen Ligocki Leads Tower
Automotive 375

Management in Action

Summary and Review 377

Management in Action 379

Topics for Discussion and Action 379

Building Management Skills:

Analyzing Failures of Leadership 379

Small Group Breakout Exercise:

Improving Leadership Effectiveness 380

Be the Manager

Managing Ethically 380

Additional Activities on the Build

Your Management Skills DVD 381

BusinessWeek Case in the

News: Siemens' New Boss:

Can He Deliver? 381

BusinessWeek Case in the News:

The Jack Welch of the Meat Aisle 383

Contents

Chapter Eleven

Effective Team Management

386



Management Snapshot
Cohesiveness and Success
at Southwest Airlines 387

Overview

Groups, Teams, and Organizational Effectiveness	388	Command Groups	395
Groups and Teams as Performance Enhancers	389	Task Forces	395
Groups, Teams, and Responsiveness to Customers	391	Self-Managed Work Teams	395
Teams and Innovation	391	Virtual Teams	396
Groups and Teams as Motivators	393	Friendship Groups	398
Types of Groups and Teams	394	Interest Groups	398
The Top-Management Team	394	Group Dynamics	398
Research and Development Teams	395	Group Size and Roles	399
		Group Leadership	400
		Group Development over Time	400
		Group Norms	401
		Group Cohesiveness	405

Chapter Twelve

Building and Managing Human Resources

418



Management Snapshot
Effectively Managing Human Resources at Semco 419

Overview

Strategic Human Resource Management	421	Training and Development	432
Overview of the Components of HRM	422	Types of Training	432
The Legal Environment of HRM	423	Types of Development	434
Recruitment and Selection	424	Transfer of Training and Development	435
Human Resource Planning	425	Performance Appraisal and Feedback	436
Job Analysis	427	Types of Performance Appraisal	436
External and Internal Recruitment	428	Who Appraises Performance?	438
The Selection Process	429	Effective Performance Feedback	439

Contents

Chapter Thirteen

Communication and Information Technology Management

454



Management Snapshot

Herman Miller's Office of the Future 455

Overview

Information and the Manager's Job

457

Attributes of Useful

Information

457

Information Systems and Technology

459

Information and Decision Making

461

Information and Control

461

Information and Coordination

462

Communication, Information, and Management

462

The Importance of Good Communication

463

The Communication Process

464

The Dangers of Ineffective Communication

466

Information Richness and Communication Media

467

Face-to-Face Communication

468

Spoken Communication

Electronically Transmitted

469

Personally Addressed

Written Communication

470

Impersonal Written

Communication

471

The Information Technology Revolution

473

The Tumbling Price of Information

473

Wireless Communications

473

Computer Networks

474

Software Developments

475

Chapter Fourteen

Operations Management: Managing Vital Operations and Processes

488



Management Snapshot

Why Toyota Is a Leader in Operations Management 489

Overview

Operations Management and Competitive Advantage

490

Improving Responsiveness to Customers

491

What Do Customers Want?

492

Designing Production

Systems to Be Responsive to

Customers

492

Improving Quality

494

Improving Efficiency

495

Facilities Layout, Flexible

Manufacturing, and Efficiency

496

Just-in-Time Inventory and

Efficiency

501

Self-Managed Work Teams

and Efficiency

502

Process Reengineering and

Efficiency

502

Operations Management: Some Remaining Issues

504

	Examples	Management in Action
Types of Management Information Systems	476	Summary and Review 481
The Organizational Hierarchy: The Traditional Information System	476	Management in Action 483
Transaction-Processing Systems	477	Topics for Discussion and Action 483
Operations Information Systems	478	Building Management Skills: Diagnosing Ineffective Communication 483
Decision Support Systems	478	Small Group Breakout Exercise: Using New Information Systems 483
Expert Systems and Artificial Intelligence	480	Be the Manager: A Problem in Communication 484
Limitations of Information Systems	480	Additional Activities on the Build Your Management Skills DVD 484
		Managing Ethically 485
	Information Technology Byte	BusinessWeek Case in the News: Blogging with the Boss's Blessing 485
	E-Stores: Amazon.com versus Bluelight.com versus Walmart.com 460	BusinessWeek Case in the News: America Online Gets Clicking 486
	Information Technology Byte	
	Collaboration Software Facilitates Communication in Teams 464	
	Information Technology Byte	
	Intel's "10 Commandments of Email" 472	
	Manager as a Person	
	How Judy Lewent Became One of the Most Powerful Women in Corporate America 479	

	Examples	Management in Action
Management Insight		Summary and Review 505
Citibank Uses CRM to Increase Customer Loyalty	493	Management in Action 507
Manager as a Person		Topics for Discussion and Action 507
How to Improve Facilities Layout	498	Building Management Skills: Managing a Production System 507
Managing Globally		Small Group Breakout Exercise: How to Compete in the Sandwich Business 507
Igus's Factory of the Future	500	Be the Manager: How to Build Flat Panel Displays 508
Management Insight		Additional Activities on the Build Your Management Skills DVD 508
United Electric's Kanban System	501	Managing Ethically 508
Ethics in Action		Case for Discussion: A "China Price" for Toyota 508
The Human Cost of Improving Productivity	504	Case for Discussion: Japan Isn't Buying the Wal-Mart Idea 510
		Appendix B: Career Development 513
		Types of Careers 514
		Career Stages 515
		Effective Career Management 517
		Video Cases 519
		Glossary 535
		Notes 548
		Photo Credits 573
		Name Index 574
		Subject Index 579
		Company Index 590

Preface

Many changes have taken place in the world of business management in the three years since we wrote this book. The managers of companies such as Enron, Tyco, Adelphia, and WorldCom and many mutual fund and insurance companies have been found guilty of acting either unethically or illegally. As a result, many of these companies have gone out of business or are close to bankruptcy, tens of thousands of employees have lost their jobs, and in 2005 the top managers of many of these companies were sentenced to long prison terms for misusing their power and privileges.

In addition, the fast-changing domestic and global environment increased the need for organizations and their managers to find new ways to respond in order to maintain and increase their performance. One of these new strategies has been the growing use of global outsourcing of information technology, services, and manufacturing jobs to countries overseas to reduce operating costs that has led to the loss of millions of jobs in the United States—and the prospect of further major job losses. Also, to increase their global competitiveness, there has been mounting pressure on managers to integrate new information technology into all aspects of organizations' operations to improve efficiency and customer responsiveness. Finally, the increasing diversity of the global workforce has made it imperative for managers to understand how and why people differ so that they can effectively manage and reap the benefits of diversity. The tasks that managers must perform efficiently and effectively have become more complex and challenging than ever before.

The second edition of *Essentials of Contemporary Management* has been significantly revised to reflect and address these challenges to managers and their organizations. Encouraged by the favorable reception of the first edition of our book, and based on the reactions and suggestions of both users and reviewers, we have reorganized some of the book's chapters and revised and updated all the book's chapters to respond to the many changes that have been taking place.

Changes in the Organization and Content of the Book

We set out to write and revise *Essentials of Contemporary Management* to distill new and classic theorizing and research into a contemporary framework that is compatible with the traditional focus on management of planning, leading, organizing, and controlling, but which also transcends this approach. We also set out to present management in a way that makes its relevance obvious even to students who might lack exposure to a “real-life” management context. Our continuing goal has been to relate management theory to real-life examples to drive home the message that management matters both because it determines how well organizations perform and because managers and organizations affect the lives of people who work inside them and people outside the organization, such as customers, communities, and shareholders.

The contemporary nature of our approach can be seen most clearly by examining our table of contents, and by perusing our treatment of management issues, especially with reference to the kinds of issues and organizations we discuss in our opening cases and the many real-life examples throughout the book.

CHAPTER REORGANIZATION As we noted in the first edition, we have some chapters that are unlike those in other essentials of management books, and in this edition we have continued to refine the way we present this material to best address contemporary issues. A major change in organization is reflected in Chapter 2, now entitled “Values, Attitudes, Emotions, and Culture: The Manager as a Person.” We have brought forward our treatment of internal organizational culture and now show how organizational culture is the outcome of the personalities, strengths, and weaknesses of managers and employees who shape all aspects of the way an organization works.

This presentation allows students to better understand that managers are people like themselves and subject to the same kinds of forces that govern their choices and actions. Students will also appreciate the challenges managers face and how, as future managers, they can successfully meet them. In addition, the material on entrepreneurship has been moved to Chapter 8, now entitled, “Control, Change, and Entrepreneurship,” which focuses on the way entrepreneurs stimulate the crucial processes of managing organizational innovation and creativity, and bring about change in a competitive global environment.

MAJOR CONTENT CHANGES WITHIN CHAPTERS Beyond this reorganization of the material, we have also revised and altered the content of the chapters. We introduce many new important models and concepts that reflect changes in management thinking. We include scores of new and updated boxes and examples that highlight the nature of the contemporary challenges facing managers today. Some highlights include: new coverage of the implications of global outsourcing; expanded coverage of information technology throughout the book, including the use of enterprise resources planning and B2B systems; inclusion of scales for measuring personality; new treatment of emotions and emotional intelligence, including a new scale that measures the latter; new treatment of organizational culture; new material on creativity; expanded focus on the sources of competitive advantage and global strategy; expanded discussion of human resource management challenges; expanded coverage of gender, emotional intelligence, and leadership; and the use of new communication systems to improve decision making.

As in the first edition, our book continues to emphasize the hands-on significance of changes in information technology for managers today. Throughout the book, we illustrate how new developments in information technology are influencing the jobs of managers and employees alike. Similarly, given its growing importance, we have increased our coverage of business ethics, and the ethics of managers, which was also a major theme of the first edition. Chapter 3 has been substantially revised to provide additional material on ethics, ethics and the law, and the

nature of ethical dilemmas, the effective management of diversity, and ways to eradicate sexual harassment. We also continue to discuss many ethical issues in our “Ethics in Action” boxes throughout the book and through our real-life ethics exercise at the end of every chapter. In all these ways we drive home to students the deep and significant ethical issues involved in management.

Emphasis on Applied Management

Our contemporary approach also is illustrated by the way we have chosen to organize and discuss contemporary management issues. We have gone to great lengths to bring the manager back into the subject matter of management. That is, we have written our chapters from the perspective of current or future managers to illustrate, in a hands-on way, the problems and opportunities managers face and how they can effectively meet these challenges. For example, in Chapter 3 we provide an integrated treatment of ethics and diversity that clearly explains their significance to practicing managers. In Chapter 6, we provide an integrated treatment of planning, strategy, and competitive advantage highlighting the crucial choices managers face as they go about performing the planning role. Throughout the text, we emphasize important issues managers face and how management theory, research, and practice can help them and their organizations be effective.

This applied approach can also clearly be seen in the last two chapters of the book that cover the topics of managing information systems, technology, and operations management, topics that have tended to be difficult to teach to new management students in an interesting and novel way. Our chapters provide a student-friendly behavioral approach to understanding the management processes entailed in information systems and operations management. As our reviewers noted, while most books’ treatment of these issues is dry and quantitative, ours comes alive with its focus on how managers can manage the people and processes necessary to give an organization a competitive advantage.

Flexible Organization

Another factor of interest to instructors concerns the way we have designed the grouping of chapters to allow instructors to teach the chapter material in the order that best suits their needs.

Instructors are not tied to the planning, organizing, leading, controlling framework, even though our presentation remains consistent with this approach.

Acknowledgments

Finding a way to integrate and present the rapidly growing literature on contemporary management and make it interesting and meaningful for students is not an easy task. In writing and revising the several drafts of *Essentials of Contemporary Management*, we have been fortunate to have had the assistance of several people who have contributed greatly to the book's final form. First, we are grateful to Kelly Lowery, our sponsoring editor, for her support and commitment to our project, and for always finding ways to provide the resources that we needed to continually improve and refine our book. Second, we are grateful to Laura Hurst Spell, our developmental editor, for so ably coordinating the book's progress and to her and Lisa Nicks, our marketing manager, for providing us with concise and timely feedback and information from professors and reviewers that has allowed us to shape the book to the needs of its intended market. We also thank Artemio Ortiz for executing an awe-inspiring design, Mary Conzachi for coordinating the production process, and Patsy Hartmangruber and Elaine Morris for providing excellent word processing and graphic support. We are grateful also to the many colleagues and reviewers who provided us with useful and detailed feedback, perceptive comments, and valuable suggestions for improving the manuscript.

Producing any competitive work is a challenge. Producing a truly market-driven textbook

requires tremendous effort beyond simply obtaining reviews on a draft manuscript. Our goal behind the development of *Essentials of Contemporary Management* was clear-cut: to be the most customer-driven essentials of management text and supplement package ever published! The favorable reception that our book has received from its users suggests that our thorough product development plan did lead to a book that has met the expectations of both faculty and students. For the new edition, we continued to add new reviewers to the over 200 faculty who originally took part in developmental activities ranging from regional focus groups to manuscript reviews and surveys. Consequently, we are confident that the changes we have made to our book and its excellent support package will even more closely meet your expectations and needs.

Our thanks to these faculty who contributed greatly to *Essentials of Contemporary Management*, Second Edition:

Andrea D. Bailey, *Moraine Valley Community College*

Judith G. Bulin, *Monroe Community College*

D. Anthony DeStadio, *Pittsburgh Technical Institute*

Marybeth Kardatzke, *North Harris Montgomery*

Community College District

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Dennis Lee Kovach, *Community College of Allegheny*

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Daniel F. Nehring, *Morehead State University*

Rieann Spence-Gale, *Alexandria Campus, Northern*

Virginia Community College

Barry L. Van Hook, *Arizona State University, Tempe*

Finally, we are grateful to two incredibly wonderful children, Nicholas and Julia, for being all that they are and the joy they bring to all who know them.

Gareth R. Jones

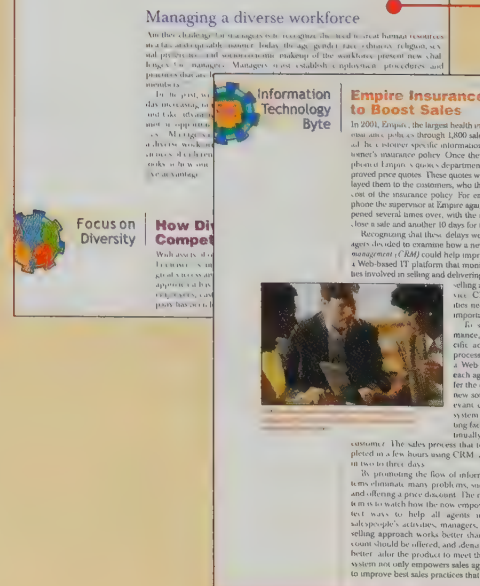
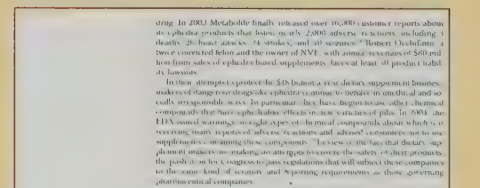
Jennifer M. George

GUIDED TOUR

RICH AND RELEVANT EXAMPLES

An important feature of our book is the way we use real-world examples and stories about managers and companies to drive home the applied lessons to students. Our reviewers were unanimous in their praise of the sheer range and depth of the rich, interesting examples we use to illustrate the chapter material and make it come alive. Moreover, unlike boxed material in other books, our boxes are seamlessly integrated into the text; they are an integral part of the learning experience, and not tacked on or isolated from the text itself. This is central to our pedagogical approach.

Each chapter opens with "Management Snapshot," which poses a chapter-related challenge and then discusses how managers in one or more organizations responded to that challenge. "A Management Snapshot" helps demonstrate the uncertainty and excitement surrounding the management process.



studies such as these make one wonder why the glass ceiling continues to hamper the progress of women in business (a topic we address later in the chapter).

Race and ethnicity

The U.S. Census Bureau typically distinguishes between the following races or ethnicities: Asian (origins in the Far East, Southeast Asia, or India); African American (origins in Africa); Native Hawaiian or Pacific Islander (origins in the Pacific Islands such as Hawaii, Guam, and Samoa); and white (origins in Europe, the Middle East, or North Africa). While ethnicity refers to a grouping of people

people and groups to effectively use human and other resources to achieve organizational goals.

Maintaining ethical and socially responsible standards

While mobilizing organizational resources, managers at all levels are under considerable pressure to increase the level at which their organizations perform.¹³ For example, top managers receive pressure from shareholders to increase the performance of the entire organization to boost the stock price, improve profits, or raise dividends. In turn, top managers may then pressure lower managers to use various ways to use organizational resources to increase efficiency or quality and thus attract new customers and earn more revenues.

Pressure to increase performance can be healthy for an organization because it causes managers to question the way the organization is working and it encourages them to find new and better ways to plan, organize, lead, and control. However, too much pressure to perform can be harmful.¹⁴ It may induce managers to behave unethically in dealings with individuals and groups both inside and outside the organization. For example, a purchasing manager for a large retail chain might buy inferior clothing at a cost-cutting measure, or to secure a large foreign contract, a sales manager in a large defense company might offer bribes to foreign officials. In 2004, the four top executives of Lucent's Korean division were fired after it was revealed they used bribery to obtain lucrative contracts for Lucent in that country.¹⁵ The issue of social responsibility concerns the obligations that a company should have toward people and groups such as customers or the community in which they operate. An example of companies that act in a socially responsible and an ethical way is described in the following "Ethics in Action."

Ethics in Action

Diet Supplement Makers and the FDA

On April 12, 2004, it became illegal to make or sell the dietary supplement ephedra in the United States.¹⁶ The Food and Drug Administration (FDA) had 6 months to obtain information from users and from makers of ephedra pills, such as Yellow Jackets and Black Boutons, that revealed over 16,000 adverse report events experienced by users of the drug. At least 40 deaths were directly related to the use of the drug, including the death of Baltimore Oriole pitcher Steven Seaver in 2003.

Ephedra has been widely available for a decade; why did it take the FDA so long to ban the use of the drug? Diet supplement makers, unlike major pharmaceutical companies, have been shielded by a 1994 law. The law does not require that the makers of dietary supplements report adverse incidents to the FDA, but it obligates the FDA to prove unreasonable public health risks.

To protect their businesses, ephedra makers like Metabolife and NVE Pharmaceuticals did not reveal complaints about their products from thousands of customers—until forced to do so by lawsuits brought by people harmed by the

Manager as a Person

New CEOs Bring Change at Avon and Lucent

Two global companies that have required a radical overhaul of their strategies in recent years are Avon, the well-known door-to-door selling cosmetics giant, and Lucent Technologies, the telecommunications company. In 2000, after several years of declining sales, Avon recognized the need for change and appointed Andrea Jung as its CEO, the first woman CEO in its history. Jung faced a tough task in trying to transform this tradition ladies company.¹⁷ She began by search for a new vision for the company.

Avon's main problem, she decided, was reaching beyond the typical 30-to-55-year-old woman who had always been its main customer. She decided to target the important 16-to-24-year-old segment and start to build brand loyalty among young customers who will become its main customer base of the future. In 2003, a new Avon division called Mark began to distribute a new line of hip cosmetics designed specifically to meet the needs of this younger market segment. To meet the sales challenge of direct distribution to customers through a personal-selling approach, Jung also decided to recruit a new generation of sales reps from the younger demographic groups. She hoped that with peers to serve, their needs, Avon's selling partners could be geared to the needs of this younger age group and its sales reps could be trained to respond to their unique needs.

The potential of this market is enormous: for the 17 million women in this segment have a total purchasing power of almost \$100 billion a year, and spend 20 percent of their income on beauty products. In 2001, Jung began to enhance actual communication, her vision for Avon to 13,000 sales representatives who gathered in Las Vegas to preview Avon's new product lines, take in some shows, and listen to the new CEO. Jung let the sales representatives know that Avon's future success depended on their efforts and that they were at the heart of Avon. Today, Avon has four million reps to find around the world, and it plans to increase the number of U.S. sales reps from 500,000 to 750,000 in the next few years.¹⁸ In 2005 Avon reported record global profits on booming worldwide sales of its growing range of makeup, soap, hair care, jewelry, and giftware.

As Lucent's performance continued to plunge, its sales fell 50 percent, sales to the telecommunications business fell 60 percent. In 2000, the company decided to bring back Patricia Russo, its former Lucent executive who had left to become the CEO of Kodak as its CEO. Russo faced a daunting task given that Lucent lost over \$10 billion in 2001. How should the first position Lucent's different business to meet the needs of its global customers while continuing to find ways to reduce costs? Russo's answer was to refocus the company's activities on three main business areas: 1) enhancing its core telecommunications services, including network design, management, and maintenance; 2) take advantage of the experience of Lucent's highly skilled engineers; 3) developing partnerships with other high-tech companies to quickly market their products. 4) handling transactions with the federal government and offering a one-stop service to all areas of government from taxes to defense. By 2004, the success of Russo's efforts was seen as Lucent finally broke even and returned to profit.

Achieving such dramatic turnarounds at these companies was also the result of the way Jung and Russo changed the way their companies were organized. To quickly take advantage of the opportunities offered by the Internet and emerging

competence. This specific set of skills, abilities, and experiences that cause one manager to perform at a higher level than another manager in a particular setting.

Manager as a Person

Steve Jobs Transforms Apple Computer

In 1976, Steven P. Jobs sold his Volkswagen van, and his partner Steven Wozniak sold his two programmable calculators. They then invested the proceeds of \$13,000 to build a computer circuit board in Jobs's garage. No program was available, which was developed into the Apple II personal computer. This in 1977 Jobs and Wozniak incorporated their new business as Apple Computer. By 1985 Apple's sales were almost \$2 billion; nevertheless, in the same year Jobs was forced out of the company, he founded, Jobs's approach to management was a big part of the reason he lost control of Apple.¹⁹

Additional in-depth examples appear in boxes throughout each chapter. "Management Insight" boxes illustrate the topics of the chapter, while the "Ethics in Action," "Managing Globally," "Focus on Diversity," and "Information Technology Byte" boxes examine the chapter topics from each of these perspectives.

These are not boxes in the traditional sense; that is, they're not disembodied from the chapter narrative. These thematic applications are fully integrated into the reading. Students will no longer be forced to decide whether to read boxed material. These features are interesting and engaging for students while bringing the chapter content to life.

NEW! "Manager as a Person" boxes focus on how real managers brought about change to their organizations. These examples within many chapters give students the opportunity to reflect on how individual managers dealt with real-life on-the-job challenges related to various chapter concepts.

EXPERIENTIAL LEARNING FEATURES

We have given considerable time and attention to developing state-of-the-art experiential end-of-chapter learning exercises that drive home the meaning of management to students. These exercises are grouped together at the end of each chapter in the section called **Management in Action**.

TOPICS FOR DISCUSSION AND ACTION A set of chapter-related questions and points for reflection, some of which ask students to research actual management issues and learn firsthand from practicing managers.

BUILDING MANAGEMENT SKILLS A self-development exercise that asks students to apply what they have learned to their own experience of organizations and managers or to the experiences of others.

SMALL GROUP BREAKOUT EXERCISE This unique exercise is designed to allow instructors in large classes to utilize interactive experiential exercises in groups of three to four students. The instructor calls on students to form into small groups simply by turning to people around them. All students participate in the exercise in class, and a mechanism is provided for the different groups to share what they have learned with one another.

BE THE MANAGER This exercise presents a realistic scenario in which a manager/organization faces some kind of challenge, problem, or opportunity and the student plays the role of the focal manager figuring out how to address the challenge based on the chapter content. These exercises provide students with a hands-on way to take an action-oriented approach to



Management in Action

Topics for Discussion and Action

Discussion

1. Describe the difference between efficiency and effectiveness, and identify real organizations that you think are, or are not, efficient and effective.
2. In what ways can managers at each of the three levels of management contribute to organizational efficiency and effectiveness?
3. Identify an organization that you believe is high-performing and one that you believe is low-performing. Give 10 reasons why you think the performance levels of the two organizations differ so much.

4. What are the building blocks of competitive advantage? Why is obtaining a competitive advantage important to managers?
5. In what ways do you think managers' jobs have changed the most over the last 10 years? Why have these changes occurred?

Action

6. Choose an organization such as a school or a bank; visit it; then list the different organizational resources it uses.
7. Visit an organization, and talk to first-line, middle, and top managers about their

respective management roles in the organization and what they do to help the organization be efficient and effective.

8. Ask a middle or top manager, perhaps someone you already know, to give examples of how he or she performs the managerial functions of planning, organizing, leading, and controlling. How much time does he or she spend in performing each function?
9. Like Mintzberg, try to find a cooperative manager who will allow you to follow him or her around for a day. List the roles the manager plays, and indicate how much time he or she spends performing them.

Building Management Skills

Thinking About Managers and Management

Think of an organization that has provided you with work experience and of the manager to whom you reported (or talk to someone who has had extensive work experience); then answer these questions.

1. Think of your direct supervisor. Of what department is he or she a member, and at what level of management is this person?
2. How do you characterize your supervisor's approach to management? For example, which particular management functions and roles does this person perform most often?
3. Do you think the functions, roles, and skills of your supervisor are appropriate for the particular job he or she performs? How could this manager improve his or her task performance? How can IT affect this?
4. How did your supervisor's approach to management affect your attitudes and

- subordinate, and how motivated were you?
5. Think of the organization and its resources. Do its managers utilize organizational resources effectively? Which resources contribute most to the organization's performance?
6. Describe the way the organization treats its human resources. How does this

7. If you could give your manager one piece of advice or change one management practice in the organization, what would it be?
8. How attuned are the managers in the organization to the need to increase efficiency, quality, innovation, or responsiveness to customers? How well do you

think the organization performs its prime goals of providing the goods or services that customers want or need the most?



Small Group Breakout Exercise

Opening a New Restaurant

Form groups of three or four people, and appoint one group member as the spokesperson who will communicate your findings to the entire class when called on by the instructor. Then discuss the following scenario.

You and your partners have decided to open a large, full-service restaurant in your local community; it will be open from 7 A.M. to 10 P.M. to serve breakfast, lunch, and dinner. Each of you is investing \$50,000 in the venture, and together you have secured a bank loan for an additional \$300,000 to begin operations. You and your partners have little experience in managing a restaurant beyond serving meals or eating in restaurants, and you now face the task of deciding how you will manage the

restaurant and what your respective roles will be.

1. Decide each partner's managerial role in the restaurant. For example, who will be responsible for the necessary departments and specific activities? Describe your managerial hierarchy.
2. Which building blocks of competitive advantage do you need to establish to help your restaurant succeed? What criteria will you use to evaluate how successfully
3. Discuss the most important decisions that must be made about (a) planning, (b) organizing, (c) leading, and (d) controlling to allow you and your partners to utilize organizational resources effectively and build a competitive advantage.
4. For each managerial function, list the issue that will contribute the most to your restaurant's success.



Be the Manager

Problems at Achieva

You have just been called in to help managers at Achieva, a fast-growing Internet software company that specializes in B2B network software. Your job is to help Achieva solve some management problems that have arisen because of its rapid growth.

Customer demand to license Achieva's software has boomed so much in just two years that more than 50 new software programmers have been added to help develop a new range of software products. Achieva's growth has been so swift

that the company still operates informally, its organizational structure is loose and flexible, and programmers are encouraged to find solutions to problems as they go along. Although this structure worked well in the past, you have been told that problems are arising.

Increasingly employees have complained that good performance is not being recognized in the organization and that they do not feel equitably treated. Moreover, employees have complained about getting managers to listen to their new ideas and to act on them. A

bad atmosphere is developing in the company, and recently several talented employees have left. Your job is to help Achieva's managers solve these problems quickly and keep the company on the fast track.

Questions

1. What kinds of organizing and controlling problems is Achieva suffering from?
2. What kinds of management changes need to be made to solve them?

solving "real" problems by applying what they've just learned in the chapter.

MANAGING ETHICALLY An exercise that presents students with an ethical scenario or dilemma and asks them, either individually or in a group, to think about the issue from an ethical perspective to understand the issues facing practicing managers.

NEW! ADDITIONAL ACTIVITIES ON THE BUILD YOUR MANAGEMENT SKILLS DVD

Do you want to put your students' leadership skills to the test, assess their emotional intelligence, or see how they would handle an employee who is not meeting expectations? You'll have opportunities to do all of this and more with Test Your Knowledge, Self-Assessment, and Manager's Hot Seat exercises on the Build Your Management Skills DVD. A list of relevant exercises on the DVD is included at the end of each chapter.

BUSINESSWEEK CASES IN THE NEWS Each chapter has two cases for analysis that are actual or shortened versions of *BusinessWeek* articles. The accompanying discussion questions encourage students to think about and analyze how real managers deal with real problems in the business world. These cases give instructors the opportunity to explore issues in more depth if they choose.

CHOOSING EXERCISES Our idea in offering instructors such a wide array of exercises to promote the learning experience is that instructors can *choose and select* from these exercises and vary them over the semester so that students can learn the meaning of management through many different avenues. These exercises complement the chapter material and have been class tested to add to the overall learning experience. Students report that they enjoy and learn from them.

Additional Activities on the Build Your Management Skills DVD

- **Test Your Knowledge:**
(1) Managerial Functions
(2) Categories of Managerial Control, and (3) Management's Historical Figures
- **Self-Assessment:** Career Planning Based on Brain Dominance and Thinking Styles Inventory
- **Manager's Hot Seat:**
(1) Project Management: Steering the Committee and
(2) Management's Historical Figures

Managing Ethically

Think about an example of unethical behavior that you observed in the past. The incident could be something you experienced as an employee or a customer or something you observed informally.

1. Either by yourself or in a group, give three reasons why you think the behavior was unethical. For example, what rules or norms were broken? Who benefited or was harmed by what took place? What was

the outcome for the people involved?

2. What steps might you take to prevent such unethical behavior and encourage people to behave in an ethical way?



Case in the News

The Hard Work in Leadership

James McNerney, Jr., has been running big outfits for a dozen years now, at General Electric (GE) and, since January 1, 2001, as chairman and chief executive of 3M. Success at these giants means more than drafting smart business plans, of course. It means getting tens of thousands of people to do what you want. But as the financial numbers at GE and 3M show, McNerney can do it.

His secret? Part of it is simply personality and upbringing: His father, Walter, instilled in him a sense of modesty and a drive to always do better, as well as passing along his own sharp intellect. Part of it is practice: McNerney has been a leader since his days at New Trier High School in Winnetka, Illinois, as president of the Tri-Skip boys club in 1966-67 and pitcher on the varsity baseball team. Another part of it is the tutelage he received during

his 18 years at GE, working for now-retired Chairman and CEO Jack Welch.

Recently, McNerney sat down in his 14th-floor suite at 3M headquarters in St. Paul, Minnesota, with *BusinessWeek* Senior Correspondent Michael Arndt. The first outsider ever to become CEO at 3M, McNerney is notoriously press shy. Yet, when it comes to management, he's voluble, talking at length on everything from motivation and corporate culture to the uses of statistical gauges like Six Sigma in personnel screening and his own style as a boss. Edited excerpts of their conversation follow.

Q: I was here two years ago, when you were still pretty new, so I'd like to start by asking you how you think you've done since then.
A: The best measurement of progress is the engagement of the

organization, the enthusiasm of the organization: Are we more one team focused on similar things, pulling together? And I feel pretty good about that.

The initiatives I talked about two years ago are exactly the same ones we have today. I believe in boring consistency of meaningful themes. Don't change the message. That's important when you're leading a big organization. Otherwise, people are waiting for the *initiative du jour*. The challenge for us is to keep refreshing them and making them meaningful.

Q: How do you achieve that team spirit?

A: My experience is that if people are convinced they're growing as they pursue company goals, that's when you get ignition. I'll use Six Sigma as an example. People are learning new ways to approach

INTEGRATED LEARNING SYSTEM

Great care was used in the creation of the supplemental materials to accompany *Essentials of Contemporary Management*. Whether you are a seasoned faculty member or a newly minted instructor, you'll find our support materials to be the most thorough and thoughtful ever created!

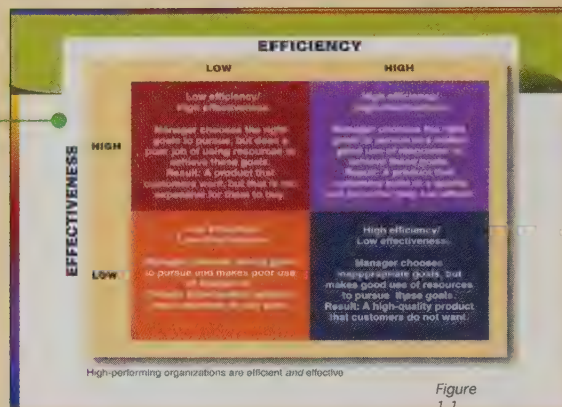
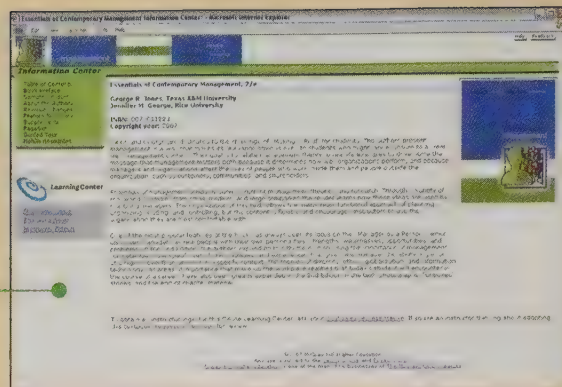
Instructor's Presentation Manager CD-ROM

This presentation CD-ROM allows instructors to easily create their own custom presentations using resources on the CD, like the Instructor's Manual and PowerPoint. The computerized test bank is also included on this CD.

Instructor's Manual Prepared by Stephanie Bibb of Chicago State University, the IM contains a chapter overview; learning objectives; key terms; resources available; notes for opening case; a lecture outline; notes for Topics for Discussion and Action questions; notes for Building Management Skills exercises; notes for Small Group Breakout exercises; notes for Be the Manager exercises; notes for Test Your Knowledge, Self-Assessment, and Manager's Hot Seat DVD exercises; notes for *BusinessWeek* cases; lecture enhancers; and video case teaching notes.

PowerPoint® Presentation

Approximately 300 slides feature reproductions of key tables and figures from the text as well as original content—prepared by Brad Cox of Midlands Tech. Now you can make your classroom more interactive with the new “Movie Example” slides and Instruction (CPS) quiz and discussion questions. “Movie Example” slides show how popular movie, such as *Office Space* and *Monty Python and the Holy Grail* can be used to generate discussion and to illustrate management concepts.



Question?

What is the specific set of abilities that allows one manager to perform at a higher level than another manager?

- A. Skill-sets
- B. SKAs
- C. Competencies
- D. Skill traits

Movie Example: Office Space

What type of manager is Bill Lumbergh in the movie “Office Space”?



Test Bank The test bank has been thoroughly reviewed, revised, and improved by Eileen Hogan of Kutztown University in response to customer feedback. There are approximately 90 questions per chapter, including true-false, multiple-choice, and essay, each tagged with level of difficulty (corresponding to Bloom's taxonomy of educational objectives), correct answer, and page references to the text.

The videos and video cases will enliven the classroom through viewing and discussing thought-provoking companies, managers, topics, and issues. Examples include Seattle's famous Pike Place Fish Market; Todd McFarlane, founder of a successful comic book and toy company; the legacy of GE's Jack Welch; and the federal government's investigation of Enron's bankruptcy, including the role played by whistle-blower Sherron Watkins. Each case provides a written overview of the video content as well as additional background information and discussion questions that encourage students to critically examine and apply chapter concepts to analyzing the case.



FOR STUDENTS

Student Study Guide

Prepared by Thomas J. Quirk of Webster University, the Study Guide has been completely updated with the goal of helping students master course content. Each chapter includes learning objectives; a chapter outline; and matching, true-false, multiple-choice, and essay questions, with answer keys including page references to the text.

NEW! Student DVD—Build Your Management Skills

This DVD makes it easy to use the latest in technology to help students hone their personal management skills. Packaged free with every new copy of the text, the Student DVD features Manager's Hot Seat exercises such as "Ethics: Let's Make a Fourth Quarter Deal" and "Change: More Pain Than Gain"; Test Your Knowledge exercises such as "Fiedler's Contingency Model of Leadership" and "Porter's Five Forces"; and Self-Assessments such as "Active Listening Skills Inventory" and "Do You Have What It Takes to Be a Leader?" An end-of-chapter section titled "Additional Activities on the Build Your Management Skills DVD" shows which exercises to use with a particular chapter. The DVD can also be ordered separately.

The Essentials of Contemporary Management Online Learning Center www.mhhe.com/jones2e

The Online Learning Center (OLC) is a Web site that follows the text chapter by chapter. OLC content is designed to reinforce and build on the text content. As students read the book, they can go online to take self-grading quizzes, review material, or work through interactive exercises. OLCs can be delivered multiple ways—professors and students can access them directly through the textbook Web site, through PageOut, or within a course management system (i.e., WebCT, Blackboard, or eCollege). In addition, PowerWeb, which brings you up-to-date articles from leading periodicals and journals, as well as current news, is now fully integrated into the OLC and is available as premium content, requiring a passcode card that is bound into new texts for free. Premium-content passcode cards are also available separately.

BusinessWeek Edition

Students can subscribe to *BusinessWeek* for a specially priced rate of \$8.25 in addition to the price of this text, when instructors order the *BusinessWeek* Edition.

The Wall Street Journal Edition

Your students can subscribe to *The Wall Street Journal* for 15 weeks at a specially priced rate of \$20 in addition to the price of the text. Students will receive the *How to Use the WSJ* handbook plus a subscription card shrink-wrapped with their new text. The subscription also gives students access to www.wsj.com.

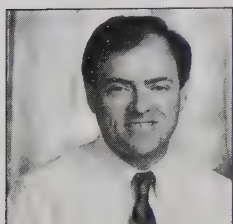
Authors

Gareth R. Jones is a Professor of Management in the Lowry Mays College and Graduate School of Business at Texas A&M University. He received his B.A. in Economics/Psychology and his Ph.D. in Management from the University of Lancaster, U.K. He previously held teaching and research appointments at the University Warwick, Michigan State University, and the University of Illinois at Urbana–Champaign. He is a frequent visitor and speaker at universities in both the United Kingdom and the United States.

He specializes in strategic management and organizational theory and is well-known for his research that applies transaction cost analysis to explain many forms of strategic and organizational behavior. He is currently interested in strategy process, competitive advantage, and information technology issues. He is also investigating the relationships between ethics, trust, and organizational culture and studying the role of affect in the strategic decision-making process.

He has published many articles in leading journals of the field and his recent work has appeared in the *Academy of Management Review*, *Journal of International Business Studies*, and *Human Relations*. An article on the role of information technology in many aspects of organizational functioning was recently published in the *Journal of Management*. One of his articles won the *Academy of Management Journal* Best Paper Award and he is one of the most prolific authors in the *Academy of Management Review*. He is or has served on the editorial boards of the *Academy of Management Review*, the *Journal of Management*, and *Management Inquiry*.

Gareth Jones has taken his academic knowledge and used it to craft leading textbooks in management, and three other major areas in the management discipline: organizational behavior, organizational theory, and strategic management. His books are widely recognized for their innovative, contemporary content, and for the clarity with which they communicate complex, real-world issues to students.



Jennifer M. George is the Mary Gibbs Jones Professor of Management and Professor of Psychology in the Jesse H. Jones Graduate School of Management at Rice University. She received her B.A. in Psychology/Sociology from Wesleyan University, her M.B.A. in Finance from New York University, and her Ph.D. in Management and Organizational Behavior from New York University. Prior to joining the faculty at Rice University, she was a Professor in the Department of Management at Texas A&M University.

She specializes in Organizational Behavior and is well known for her research on mood and emotion in the workplace, their determinants, and their effects on various individual- and group-level work outcomes. Currently, she is exploring how individual and contextual characteristics interact to promote or inhibit creativity in organizations. She is the author of many articles in leading peer-reviewed journals such as the *Academy of Management Journal*, *Academy of Management Review*, *Journal of Applied Psychology*, *Organizational Behavior and Human Decision Processes*, *Journal of Personality and Social Psychology*, and *Psychological Bulletin*. One of her papers won the Academy of Management's Organizational Behavior Division Outstanding Competitive Paper Award and another paper won the *Human Relations* Best Paper Award. She is, or has been, on the editorial review boards of the *Journal of Applied Psychology*, *Academy of Management Journal*, *Academy of Management Review*, *Administrative Science Quarterly*, *Journal of Management*, *Organizational Behavior and Human Decision Processes*, *International Journal of Selection and Assessment*, and *Journal of Managerial Issues*; was a consulting editor for the *Journal of Organizational Behavior*; and was a member of the SIOP Organizational Frontiers Series editorial board. She is a Fellow in the American Psychological Association, the American Psychological Society, and the Society for Industrial and Organizational Psychology and a member of the Society for Organizational Behavior. Professor George is currently an Associate Editor for the *Journal of Applied Psychology*.



CHAPTER

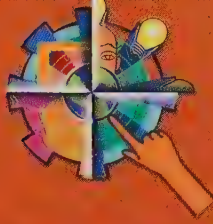
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The Management Process Today

Learning Objectives

After studying this chapter, you should be able to:

- Describe what management is, why management is important, what managers do, and how managers utilize organizational resources efficiently and effectively to achieve organizational goals.
- Distinguish among planning, organizing, leading, and controlling (the four principal managerial functions), and explain how managers' ability to handle each one can affect organizational performance.
- Differentiate among three levels of management, and understand the responsibilities of managers at different levels in the organizational hierarchy.
- Identify the roles managers perform, the skills they need to execute those roles effectively, and the way new information technology is affecting these roles and skills.
- Discuss the principal challenges managers face in today's increasingly competitive global environment.



Management Snapshot

Different Approaches to Management at The Home Depot and Lowe's: What Is High-Performance Management?

Home Depot shot to fame when its founders, Bernie Marcus and Arthur Blank, developed a new concept for a home improvement store. Their vision was to fill a warehouse-type store from floor to ceiling with a wide range of low-priced products and to provide excellent customer service. Home Depot's well-informed salespeople offered customers knowledgeable advice and they even conducted classes showing do-it-yourselfers how to install bathrooms or tile floors, for example. According to Home Depot's founders, even the stores' somewhat "scruffy" appearance was deliberate because Marcus and Blank wanted them to look like busy warehouses to assure customers they were getting rock bottom prices.¹ During 1979, Marcus and Blank opened three stores in Atlanta, Georgia, employing 200 associates and earning \$7 million in sales. By 1989, Home Depot was no longer a small business, with a total of 118 stores that employed 17,500 associates and earned \$2.7 billion in sales. By 2000, Home Depot had grown to become the market leader with over 1,100 stores and over \$47 billion in sales. Home Depot's high profits led its stock to soar in value.

Home Depot's early success began to change in 2000 when it experienced intense competition from Lowe's, a rapidly expanding chain of home improvement stores.² While Lowe's stores were also warehouse-like, its



Faced with intense competition in recent years from Lowe's, Home Depot hopes its new line of fashionable bathroom hardware and kitchen fixtures will help boost the company's bottom line.

managers had a different vision for their stores. Lowe's managers felt stores should be brightly lit, have wide aisles, and provide an attractive shopping experience—a very different idea from Home Depot's founders' "warehouse" concept. Lowe's did imitate Home Depot's strategy to provide excellent customer service and provide employees with extensive training. Lowe's product mix appealed more to female customers who make many of the big-spending decisions such as new kitchens or bathrooms.

Home Depot's other major problem was that one of its founders, Arthur Blank, became its new CEO in 1997, and assumed direct management of the company. Under his leadership operating costs rose sharply as the costs of managing an ever expanding U.S. store network increased in part because Blank allowed each store manager to decide what products to offer customers. This policy led to stocking a wider and wider range of products—which proved to be very expensive.³

In 2002, investors realized Home Depot was in trouble. Its profitability was falling sharply because of poor management decisions while Lowe's profitability was rising because of good management decisions. Home Depot's stock dropped *53 percent* in 2002, which wiped billions off its market value. A new CEO, Robert Nardelli, was hired to solve Home Depot's rapidly worsening problems. Nardelli decided to reduce operating costs by centralizing purchasing decisions and to limit

the range of products the stores carried. Nardelli instructed store managers to hire more part-timers to reduce the costs of health benefits and pensions.

As Nardelli discovered, reducing operating costs does not lead to higher sales if customers also lose interest in a company's products. Centralized purchasing decisions meant local store managers could not stock the products that best met the needs of their customers. To streamline its range of products Home Depot stopped stocking the newest, most up-to-date products customers wanted. The stores' new part-time employees had limited home improvement knowledge and they became increasingly unable to answer customers' questions.

Realizing his error, in 2003, Nardelli decided once again to change how Home Depot does business in order to respond to Lowe's competitive threat. Nardelli invested \$500 million to buy new inventory such as fashionable bathroom hardware, kitchen fixtures, and rugs to update his company's product line. New employee-training programs were introduced to rebuild Home Depot's reputation for great customer service. While these new moves increased costs, they also significantly increased sales—especially by customers who bought expensive big-ticket items. By 2005 it was clear Nardelli had fashioned a successful new way for his company to compete against Lowe's. As Home Depot's profits increased so has its stock price.⁴

Overview

The history of The Home Depot's ups and downs illustrates many of the challenges facing people, including those who found small businesses, when they become managers: Managing a large company is a complex activity, and effective managers must possess many kinds of skills, knowledge, and abilities. Management is an unpredictable process. Making the right decision is difficult; even effective managers often make mistakes, but the most effective managers are the ones, like Nardelli, who learn from their mistakes and continually strive to find ways to help their companies increase their competitive advantage and performance.

In this chapter, we look at what managers do and what skills and abilities they must develop if they are to manage their organizations successfully over time. We also identify the different kinds of managers that organizations need and the skills and abilities they must develop if they are to be successful. Finally, we identify

some of the challenges that managers must address if their organizations are to grow and prosper.

What Is Management?

management The planning, organizing, leading, and controlling of human and other resources to achieve organizational goals efficiently and effectively.

When you think of a manager, what kind of person comes to mind? Do you see someone who, like Bob Nardelli, can determine the future prosperity of a large for-profit company? Or do you see the administrator of a not-for-profit organization, such as a school, library, or charity, or the person in charge of your local Wal-Mart store or McDonald's restaurant, or the person *you* answer to if you have a part-time job? What do all these managers have in common? First, they all work in organizations. *Organizations* are collections of people who work together and coordinate their actions to achieve a wide variety of *goals*, or desired future outcomes.⁵ Second, as managers, they are the people responsible for supervising the use of an organization's human and other resources to achieve its goals. **Management**, then, is the planning, organizing, leading, and controlling of human and other resources to achieve organizational goals efficiently and effectively. An organization's *resources* include assets such as people and their skills, know-how, and knowledge; machinery; raw materials; computers and information technology; and financial capital.

Achieving high performance: a manager's goal

One of the most important goals that organizations and their members try to achieve is to provide some kind of good or service that customers desire. The principal goal of CEO Bob Nardelli is to manage The Home Depot so that the stores stock the kinds of home improvement products customers want and sales associates provide customers with excellent advice and quality service. The principal goal of doctors, nurses, and hospital administrators is to increase their hospital's ability to make sick people well. Likewise, the principal goal of each McDonald's restaurant manager is to produce burgers, fries, and shakes that people want to pay for and eat.

organizational performance A measure of how efficiently and effectively a manager uses resources to satisfy customers and achieve organizational goals.

Organizational performance is a measure of how efficiently and effectively managers use resources to satisfy customers and achieve organizational goals. Organizational performance increases in direct proportion to increases in efficiency and effectiveness (see Figure 1.1, page 6).

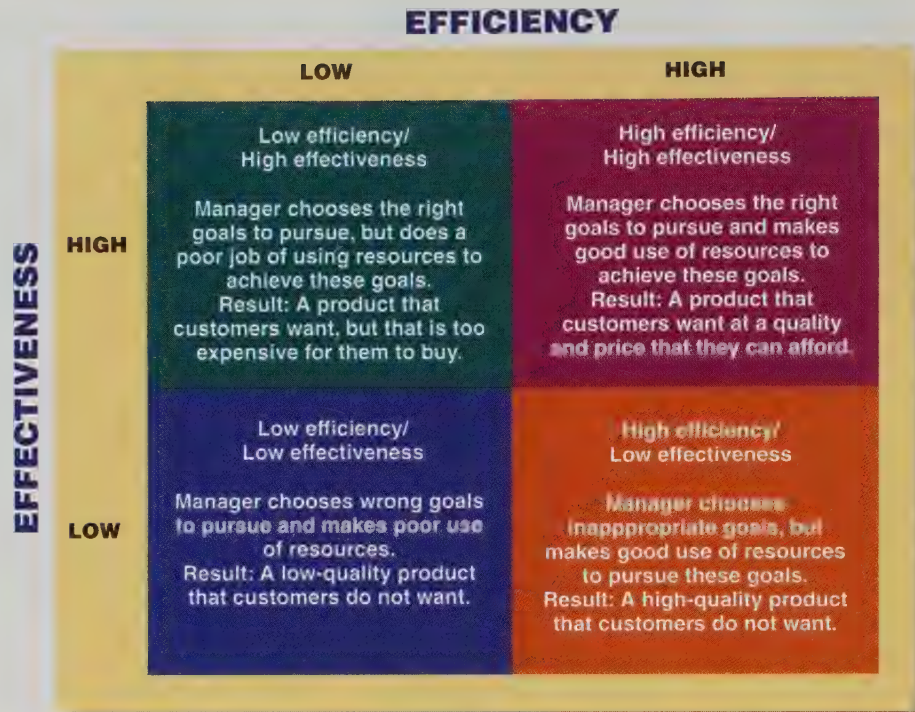
efficiency A measure of how well or how productively resources are used to achieve a goal.

Efficiency is a measure of how well or how productively resources are used to achieve a goal.⁶ Organizations are efficient when managers minimize the amount of input resources (such as labor, raw materials, and component parts) or the amount of time needed to produce a given output of goods or services. For example, McDonald's developed a more efficient fat fryer that not only reduces the amount of oil used in cooking by 30 percent but also speeds up the cooking of french fries. Bob Nardelli instructed Home Depot's store managers to reduce the range of products sold in their stores to reduce costs, while better meeting the needs of the customers. A manager's responsibility is to ensure that an organization and its members perform as efficiently as possible all the activities needed to provide goods and services to customers.

effectiveness A measure of the appropriateness of the goals an organization is pursuing and of the degree to which the organization achieves those goals.

Effectiveness is a measure of the appropriateness of the goals that managers have selected for the organization to pursue and of the degree to which the organization achieves those goals. Organizations are effective when managers choose appropriate

Figure 1.1
Efficiency,
Effectiveness,
and Performance
in an Organization



High-performing organizations are efficient *and* effective.

goals and then achieve them. Some years ago, for example, managers at McDonald's decided on the goal of providing breakfast service to attract more customers. The choice of this goal has proved very smart, for sales of breakfast food now account for more than 30 percent of McDonald's revenues. Nardelli's goal is to ensure a constant flow of state-of-the-art home improvement products into his stores. High-performing organizations, such as The Home Depot, McDonald's, Wal-Mart, Intel, Accenture, and the March of Dimes, are simultaneously efficient and effective, as shown in Figure 1.1. Effective managers are those who choose the right organizational goals to pursue and have the skills to utilize resources efficiently.

Why study management?

Today, more students are competing for places in business courses than ever before; the number of people wishing to pursue Master of Business Administration (MBA) degrees—today's passport to an advanced management position—either on campus or from online universities is at an all-time high. Why is the study of management currently so popular?⁷

First, in any society or culture resources are valuable and scarce, so the more efficient and effective use that organizations can make of those resources, the greater the relative well-being and prosperity of people in that society. Because managers are the people who decide how to use many of a society's most valuable resources—its skilled employees, raw materials like oil and land, computers and information systems, and financial assets—they directly impact the well-being of a society and the people in it. Understanding what managers do and how they do it is of central importance to understanding how a society works and how it creates wealth.

Second, although most people are not managers, and many may never intend to become managers, almost all of us encounter managers because most people have jobs and bosses. Moreover, many people today are working in groups and teams and have to deal with co-workers. Studying management helps people to deal with their bosses and their co-workers. It reveals how to understand other people at work and make decisions and take actions that win the attention and support of the boss. Management also teaches people not yet in positions of authority how to lead co-workers, solve conflicts between them, and increase team performance.

Third, in any society, people are in competition for a very important resource—a well-paying job and an interesting and satisfying career—and understanding management is one important path toward obtaining such a position. In general, jobs become more interesting the more complex or responsible they are. Any person who desires a motivating job that changes over time might therefore do well to develop management skills and become promotable. A person who has been working for several years and then returns to school for an MBA can usually, after earning the degree, find a more interesting, satisfying job and one that pays significantly more than the previous job. Moreover, salaries increase rapidly as people move up the organizational hierarchy, whether it is a school system, a large for-profit business organization, or a not-for-profit charitable or medical institution.

Indeed, the salaries paid to top managers are enormous. For example, the CEOs and other top executives or managers of companies such as Home Depot, Dell, Walt Disney, GE, and McDonald's receive millions in actual salary each year. However, even more staggering is the fact that most top executives also receive stock or shares in the company they manage, as well as stock options that give them the right to sell these shares at a certain time in the future.⁸ If the value of the stock goes up, then the managers keep the difference between the price they obtained the stock option for and what it is worth later. Michael Eisner, CEO of Walt Disney, for example, received stock options that were worth \$1 billion when Disney's stock soared in the 1990s. When Steve Jobs again became CEO of Apple, he decided he would accept a salary of only \$1 a year. However, Jobs was also awarded stock options that were worth over \$300 million by 2005.⁹ These incredible amounts of money provide some indication of both the responsibilities and the rewards that accompany the achievement of high management positions in major companies. What is it that managers actually do to receive such rewards?¹⁰

Managerial Functions

The job of management is to help an organization make the best use of its resources to achieve its goals. How do managers accomplish this objective? They do so by performing four essential managerial functions: *planning*, *organizing*, *leading*, and *controlling* (see Figure 1.2). The arrows linking these functions in Figure 1.2 suggest the sequence in which managers typically perform the functions. French manager Henri Fayol first outlined the nature of these managerial activities around the turn of the twentieth century in *General and Industrial Management*, a book that remains the classic statement of what managers must do to create a high-performing organization.¹¹

Managers at all levels and in all departments—whether in small or large organizations, for-profit or not-for-profit organizations, or organizations that operate in one country or throughout the world—are responsible for performing these four functions, which we look at next. How well managers perform these functions determines how efficient and effective their organizations are.

Figure 1.2
Four Functions
of Management



Planning

planning Identifying and selecting appropriate goals and courses of action; one of the four principal functions of management.

Planning is a process that managers use to identify and select appropriate goals and courses of action. Three steps in the planning process are (1) deciding which goals the organization will pursue, (2) deciding what courses of action to adopt to attain those goals, and (3) deciding how to allocate organizational resources to attain those goals. How well managers plan determines how effective and efficient the organization is—its performance level.¹²

As an example of planning in action, consider the situation confronting Michael Dell, CEO of Dell Computer, the most profitable PC maker and Apple's main competitor.¹³ In 1984, the 19-year-old Dell saw an opportunity to enter the PC market by assembling PCs and then selling them directly to customers. Dell began to plan how to put his idea into practice. First, he decided that his goal was to sell an inexpensive PC, to undercut the prices of companies like Compaq and Apple. Second, he had to decide on a course of action to achieve this goal. He decided to sell directly to customers by telephone and to bypass expensive computer stores that sold Compaq and Apple PCs. He also had to decide how to obtain low-cost components and how to tell potential customers about his products. Third, he had to decide how to allocate his limited funds (he only had \$5,000) to buy labor and other resources. He chose to hire three people and work with them around a table to assemble his PCs.

Thus, to put his vision of making and selling PCs into practice, Dell had to plan, and as his organization grew, his plans changed and became progressively more complex. Dell and his managers are continually planning how to help the company maintain its position as the biggest and highest-performing PC maker. In 2003, Dell announced it would begin to sell printers and personal digital assistants (PDAs); this brought it into direct competition with Hewlett-Packard (HP), the leading printer maker, and Palm One, the maker of the Palm Pilot. In 2003, Dell also brought out

Michael Dell sits in the dorm room at the University of Texas, Austin, where he launched his personal computer company as a college freshman. The room is now occupied by freshmen Russell Smith (left) and Jacob Frith, both from Plano, Texas.



its own Internet music player, the Digital Jukebox, to compete against Apple's iPod, and in 2005 it announced it would sell a new line of low-priced servers and storage devices to compete with those offered by HP and Sun.

strategy A cluster of decisions about what goals to pursue, what actions to take, and how to use resources to achieve goals.

As Dell's actions suggest, the outcome of planning is a **strategy**, a cluster of decisions concerning what organizational goals to pursue, what actions to take, and how to use resources to achieve goals. The decisions that were the outcome of Michael Dell's planning formed a *low-cost strategy*. A low-cost strategy is a way of obtaining customers by making decisions that allow the organization to produce its goods or services cheaply so that prices can be kept low. Dell has been constantly refining this strategy and exploring new strategies to reduce costs. Dell has become the most profitable PC maker as a result of its low-cost strategy, and it is hoping to repeat its success in the music player business. By contrast, Apple Computer's current strategy is to deliver new, exciting, and different computer and digital products, such as the iPod, to its customers—a strategy known as *differentiation*. The mini iPod and photo iPod were developed for people on the go, for example; they have unique, easy-to-use controls and come in a variety of bright contemporary colors.¹⁴

Planning is a difficult activity because normally what goals an organization should pursue and how best to pursue them—which strategies to adopt—is not immediately clear. Managers take risks when they commit organizational resources to pursue a particular strategy. Either success or failure is a possible outcome of the planning process. Dell succeeded spectacularly, but many other PC makers either went out of business (such as Packard Bell and Digital) or lost huge sums of money (like IBM and AT&T) trying to compete in this industry. In Chapter 8 we focus on the planning process and on the strategies organizations can select to respond to opportunities or threats in an industry. The story of Patricia Russo's rise to power at Lucent illustrates well how important planning and strategy making are to a manager's career success.



Manager as a Person

New CEOs Bring Change at Avon and Lucent

Two global companies that have required a radical overhaul of their strategies in recent years are Avon, the well-known door-to-door selling cosmetics giant, and Lucent Technologies, the telecommunications company. In 2000, after several years of declining sales, Avon recognized the need for change and appointed Andrea Jung as its CEO, the first woman CEO in its history. Jung faced a tough task in trying to transform this tradition-laden company.¹⁵ She began by searching for a new vision for the company.

Avon's main problem, she decided, was reaching beyond the typical 30-to-55-year-old woman who had always been its main customer. She decided to target the important 16-to-24-year-old segment and attract and build brand loyalty among young customers who will become its main customer base of the future. In 2003, a new Avon division called *Mark* began to distribute a new line of hip cosmetics designed specifically to meet the needs of this younger market segment. To meet the sales challenge of direct distribution to customers through a personal selling approach, Jung also decided to recruit a new generation of sales reps from the younger demographic groups. She hoped that with peers to serve their needs, Avon's selling parties could be geared to the needs of this younger age group and its sales reps could be trained to respond to their unique needs.

The potential of this market is enormous for the 17 million women in this segment have a total purchasing power of almost \$100 billion a year, and spend 20 percent of their income on beauty products. In 2001, Jung began to enthusiastically communicate her vision for Avon to 13,000 sales representatives who gathered in Las Vegas to preview Avon's new product lines, take in some shows, and listen to the new CEO. Jung let the sales representatives know that Avon's future success depended on their efforts and that they were at the heart of Avon.

Today, Avon has four million reps located around the world, and it plans to increase the number of U.S. sales reps from 500,000 to 750,000 in the next few years.¹⁶ In 2005 Avon reported record global profits on booming worldwide sales of its growing range of makeup, soaps, haircare, jewelry, and other products.

As Lucent's performance continued to plunge, because of shrinking sales due to the telecommunications bust in the early 2000s, the company decided to bring back Patricia Russo (a former Lucent executive who had left to become the COO of Kodak) as its CEO. Russo faced a daunting task given that Lucent lost over \$16 billion in 2001.¹⁷ How should she best position Lucent's different businesses to meet the needs of its global customers while continuing to find ways to reduce costs? Russo's answer was to refocus the company's activities on three main business areas: (1) enhancing telecommunications services, involving network design, management, and maintenance, to take advantage of the experience of Lucent's highly skilled engineers; (2) developing partnerships with other high-tech companies to jointly market their products; (3) boosting Lucent's ties with the federal government and offering a streamlined service to all areas of government from taxes to defense.¹⁸ By 2004, the success of Russo's efforts was seen as Lucent finally broke even and returned to profit.¹⁹

Achieving such dramatic turnarounds at these companies was also the result of the way Jung and Russo changed the way their companies were organized. To quickly take advantage of the opportunities offered by the Internet and emerging



Avon CEO Andrea Jung has given the company a “makeover” by focusing hiring a younger sales force and embracing technology with increased Internet sales.

information technology, both executives created a new organizing plan that focused on the need to develop and sell new products. At first, Avon’s army of sales reps had viewed the Internet as a way of bypassing them and costing them their commissions. However, Jung worked hard to show reps that their company cared about them, and that customers who bought over the Internet would very likely prove to be good prospects for their personal selling approach once customers had bought and tried Avon’s products. Jung’s predictions proved correct, Internet sales increased, not decreased, their commissions and its sales reps now actively embrace the new possibilities the Internet has opened up for their personal selling approach. In Lucent’s case, utilizing the Internet meant streamlining services to customers such as large corporations and the federal government.

In this way, Lucent could continuously monitor the performance of its customers’ networks to prevent breakdowns in their operations.

Jung’s flair and drive for making the most of Avon’s resources is communicated clearly to reps in her leadership style. This is based on using her personality and charisma to convince sales reps that if they continue to work toward achieving her vision of making Avon the number one shopping place for women around the globe, the possibilities for them are endless. Russo, on her part noted that her return to Lucent was because “This was the only job I considered leaving for. It is in an industry I know, with customers and people I know.” Her leadership approach is based on clearly communicating to her managers that her priorities are to improve relationships with customers and with other companies to find new ways to create valued products and services. For both CEOs, planning and organizing are vital functions that they insist must be continuously worked on by managers at all levels of the company.

organizing

Structuring working relationships in a way that allows organizational members to work together to achieve organizational goals; one of the four principal functions of management.

organizational structure

A formal system of task and reporting relationships that coordinates and motivates organizational members so that they work together to achieve organizational goals.

Organizing

Organizing is a process that managers use to establish a structure of working relationships that allow organizational members to interact and cooperate to achieve organizational goals. Organizing involves grouping people into departments according to the kinds of job-specific tasks they perform. In organizing, managers also lay out the lines of authority and responsibility between different individuals and groups, and they decide how best to coordinate organizational resources, particularly human resources.

The outcome of organizing is the creation of an **organizational structure**, a formal system of task and reporting relationships that coordinates and motivates

members so that they work together to achieve organizational goals. Organizational structure determines how an organization's resources can be best used to create goods and services. As Dell Computer grew, for example, Michael Dell faced the issue of how to structure the organization. Early on he was hiring 100 new employees a week and deciding how to design his managerial hierarchy to best motivate and coordinate managers' activities. As his organization grew, he and his managers created progressively more complex kinds of organizational structures to help it achieve its goals. We examine the organizing process in detail in Chapters 9 through 11.

Leading

leading Articulating a clear vision and energizing and enabling organizational members so that they understand the part they play in achieving organizational goals; one of the four principal functions of management.

In **leading**, managers not only articulate a clear vision for organizational members to follow but also energize and enable organizational members so that they understand the part they play in achieving organizational goals. Leadership depends on the use of power, influence, vision, persuasion, and communication skills to coordinate the behaviors of individuals and groups so that their activities and efforts are in harmony and to encourage employees to perform at a high level. The outcome of leadership is a high level of motivation and commitment among organizational members. Employees at Dell Computer, for example, responded well to Michael Dell's hands-on leadership style, which has resulted in a hardworking, committed workforce. Similarly, Home Depot's store managers now recognize how important it was that Bob Nardelli centralized purchasing to reduce costs. We discuss the issues involved in managing and leading individuals and groups in Chapters 9 through 12.

Controlling

controlling Evaluating how well an organization is achieving its goals and taking action to maintain or improve performance; one of the four principal functions of management.

In **controlling**, managers evaluate how well an organization is achieving its goals and take action to maintain or improve performance. For example, managers monitor the performance of individuals, departments, and the organization as a whole to see whether they are meeting desired performance standards. Michael Dell learned early in his career how important this is. If standards are not being met, managers take action to improve performance.

The outcome of the control process is the ability to measure performance accurately and regulate organizational efficiency and effectiveness. To exercise control, managers must decide which goals to measure—perhaps goals pertaining to productivity, quality, or responsiveness to customers—and then they must design information and control systems that will provide the data they need to assess performance. The controlling function also allows managers to evaluate how well they themselves are performing the other three functions of management—planning, organizing, and leading—and to take corrective action.

Michael Dell had difficulty establishing effective control systems because his company was growing so rapidly and he lacked experienced managers. In 1988 Dell's costs soared because no controls were in place to monitor inventory, which had built up rapidly. In 1993 financial problems arose because of ill-advised foreign currency transactions. In 1994 Dell's new line of laptop computers crashed because poor quality control resulted in defective products, some of which caught fire. To solve these and other control problems, Dell hired experienced managers to put the right control systems in place. As a result, by 1998 Dell was able to make

computers for about 10 percent less than its competitors, creating a major source of competitive advantage. By 2001 Dell had become so efficient it was driving its competitors out of the market because it had realized a 15 to 20 percent cost advantage over them.²⁰ By 2003 it was the biggest PC maker in the world. Controlling, like the other managerial functions, is an ongoing, fluid, always changing process that demands constant attention and action. We cover the most important aspects of the control function in Chapters 8, 13, and 14.

The four managerial functions—planning, organizing, leading, and controlling—are essential to a manager's job. At all levels in a managerial hierarchy, and across all departments in an organization, effective management means making decisions and managing these four activities successfully.

Types of Managers

To perform efficiently and effectively, organizations employ three types of managers—first-line managers, middle managers, and top managers—arranged in a hierarchy (see Figure 1.3, page 13). Typically, first-line managers report to middle managers, and middle managers report to top managers. Managers at each level have different but related responsibilities for utilizing organizational resources to increase efficiency and effectiveness. These three types of managers are grouped into departments (or *functions*) according to their specific job responsibilities. A **department**, such as manufacturing, accounting, or engineering, is a group of people who work together and possess similar skills or use the same kind of knowledge, tools, or techniques to perform their jobs. Within each department are all three levels of management. Next, we examine the reasons why organizations use a hierarchy of managers and group them into departments. We then examine some recent changes taking place in managerial hierarchies.

department A group of people who work together and possess similar skills or use the same knowledge, tools, or techniques to perform their jobs.

Levels of management

As just discussed, organizations normally have three levels of management: first-line managers, middle managers, and top managers.

Figure 1.3
Types of
Managers



first-line manager

A manager who is responsible for the daily supervision of nonmanagerial employees.

middle manager

A manager who supervises first-line managers and is responsible for finding the best way to use resources to achieve organizational goals.

top manager

A manager who establishes organizational goals, decides how departments should interact, and monitors the performance of middle managers.

FIRST-LINE MANAGERS At the base of the managerial hierarchy are **first-line managers**, often called *supervisors*. They are responsible for the daily supervision of the nonmanagerial employees who perform many of the specific activities necessary to produce goods and services. First-line managers work in all departments or functions of an organization.

Examples of first-line managers include the supervisor of a work team in the manufacturing department of a car plant, the head nurse in the obstetrics department of a hospital, and the chief mechanic overseeing a crew of mechanics in the service function of a new-car dealership. At Dell Computer, first-line managers include the supervisors responsible for controlling the quality of Dell computers or the level of customer service provided by Dell's telephone salespeople. When Michael Dell started his company, he personally controlled the computer assembly process and thus performed as a first-line manager or supervisor.

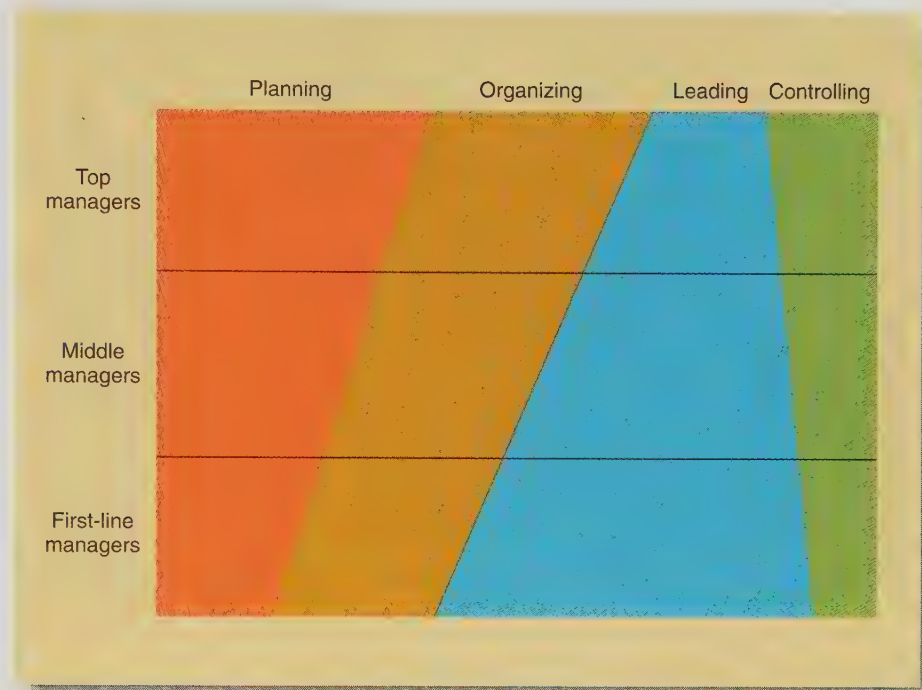
MIDDLE MANAGERS Supervising the first-line managers are **middle managers**, responsible for finding the best way to organize human and other resources to achieve organizational goals. To increase efficiency, middle managers find ways to help first-line managers and nonmanagerial employees better utilize resources to reduce manufacturing costs or improve customer service. To increase effectiveness, middle managers evaluate whether the goals that the organization is pursuing are appropriate and suggest to top managers ways in which goals should be changed. Very often, the suggestions that middle managers make to top managers can dramatically increase organizational performance. A major part of the middle manager's job is developing and fine-tuning skills and know-how, such as manufacturing or marketing expertise, that allow the organization to be efficient and effective. Middle managers make thousands of specific decisions about the production of goods and services: Which first-line supervisors should be chosen for this particular project? Where can we find the highest-quality resources? How should employees be organized to allow them to make the best use of resources?

Behind a first-class sales force look for the middle managers responsible for training, motivating, and rewarding the salespeople. Behind a committed staff of high school teachers look for the principal who energizes them to find ways to obtain the resources they need to do outstanding and innovative jobs in the classroom.

TOP MANAGERS In contrast to middle managers, **top managers** are responsible for the performance of *all* departments.²¹ They have *cross-departmental responsibility*. Top managers establish organizational goals, such as which goods and services the company should produce; they decide how the different departments should interact; and they monitor how well middle managers in each department utilize resources to achieve goals.²² Top managers are ultimately responsible for the success or failure of an organization, and their performance (like that of Bob Nardelli and Patricia Russo) is continually scrutinized by people inside and outside the organization, such as other employees and investors.²³

The *chief executive officer (CEO)* is a company's most senior and important manager, the one to whom all other top managers report. Today, the term *chief operating officer (COO)* is often used to refer to the top manager who is being groomed to take over as CEO when the current CEO retires or leaves the company. Together, the CEO and COO are responsible for developing good working relationships among the top managers of various departments (manufacturing and marketing, for example); usually top managers have the title "vice president." A central concern

Figure 1.4
Relative Amount
of Time That
Managers Spend
on the Four
Managerial
Functions



top-management team A group composed of the CEO, the COO, and the heads of the most important departments.

of the CEO is the creation of a smoothly functioning **top-management team**, a group composed of the CEO, the COO, and the department heads most responsible for helping achieve organizational goals.²⁴

The relative importance of planning, organizing, leading, and controlling—the four managerial functions—to any particular manager depends on the manager's position in the managerial hierarchy.²⁵ The amount of time that managers spend planning and organizing resources to maintain and improve organizational performance increases as they ascend the hierarchy (see Figure 1.4).²⁶ Top managers devote most of their time to planning and organizing, the functions so crucial to determining an organization's long-term performance. The lower that managers' positions are in the hierarchy, the more time the managers spend leading and controlling first-line managers or nonmanagerial employees.

Areas of managers

Because so much of a manager's responsibility is to acquire and develop critical resources, managers are typically members of specific departments.²⁷ Managers inside a department possess job-specific skills and are known as, for example, marketing managers or manufacturing managers. As Figure 1.3 indicates, first-line, middle, and top managers, who differ from one another by virtue of their job-specific responsibilities, are found in each of an organization's major departments. Inside each department, the managerial hierarchy also emerges.

At Dell Computer, for example, Michael Dell hired experts to take charge of the marketing, sales, and manufacturing departments and to develop work procedures to help first-line managers control the company's explosive sales growth.

The head of manufacturing quickly found that he had no time to supervise computer assembly, so he recruited manufacturing middle managers from other companies to assume this responsibility.

Recent changes in managerial hierarchies

The tasks and responsibilities of managers at different levels have been changing dramatically in recent years. Two major factors that have led to these changes are global competition and advances in new information technology (IT) and in e-commerce. Stiff competition for resources from organizations both at home and abroad has put increased pressure on all managers to improve efficiency, effectiveness, and organizational performance. Increasingly, top managers are encouraging lower-level managers to look beyond the goals of their own departments and take a cross-departmental view to find new opportunities to improve organizational performance, as Michael Dell and Bob Nardelli have done. New information technologies give managers at all levels access to more and better information and improve their ability to plan, organize, lead, and control; this has also revolutionized the way the managerial hierarchy works.²⁸

RESTRUCTURING AND OUTSOURCING To take advantage of IT and e-commerce and their ability to reduce operating costs, CEOs and top-management teams have been restructuring organizations and outsourcing specific organizational activities to reduce the number of employees on the payroll.

restructuring

Downsizing an organization by eliminating the jobs of large numbers of top, middle, and first-line managers and nonmanagerial employees.

Restructuring involves the use of information technology to downsize an organization or shrink its operations by eliminating the jobs of large numbers of top, middle, or first-line managers and nonmanagerial employees. For example, IT allows fewer employees to perform a given task because it increases each person's ability to process information and make decisions more quickly and accurately. U.S. companies are spending over \$50 billion a year on advanced IT that improves efficiency and effectiveness. We discuss IT's many dramatic effects on management in Chapter 13.

Restructuring, however, can produce some powerful negative outcomes. IT can reduce the morale of the remaining employees, who are worried about their own job security. And top managers of many downsized organizations are realizing that they downsized too far, because employees complain they are overworked and because more customers complain about poor-quality service.²⁹

outsourcing

Contracting with another company, usually abroad, to have it perform an activity the organization previously performed itself.

Outsourcing involves contracting with another company, usually in a low-cost country abroad, to have it perform an activity the organization previously performed itself, such as manufacturing or marketing. Outsourcing promotes efficiency by reducing costs and by allowing an organization to make better use of its remaining resources. The need to respond to low-cost global competition has speeded outsourcing dramatically in the 2000s. Three million U.S. jobs in the manufacturing sector have been lost since 2000 as companies moved their operations to countries such as China, Taiwan, and Malaysia. Tens of thousands of high-paying jobs in IT have moved to countries like India and Russia, where programmers work for one-third the salary of those in the United States.

Large for-profit organizations today typically employ 10 to 20 percent fewer employees than they did 10 years ago because of restructuring and outsourcing.

Employees of 24/7 Customer in Bangalore provide phone support for United States and United Kingdom clients and must work through the night. It is estimated that up to 1.6 million U.S. jobs will shift offshore by 2010; however, the U.S. Bureau of Labor Statistics expects 22 million new jobs will be created by other industries.



General Motors, IBM, AT&T, HP, Dell, and Du Pont are among the thousands of organizations that have streamlined their operations to increase efficiency and effectiveness. The argument is that the managers and employees who have lost their jobs will find employment in new and growing U.S. organizations where their skills and experience will be better utilized. For example, the millions of manufacturing jobs that have been lost overseas will soon be replaced by higher-paying U.S. jobs in the service sector that are made possible because of the growth in global trade.

EMPOWERMENT AND SELF-MANAGED TEAMS Another major change in management has taken place at the level of first-line managers, who typically supervise the employees engaged in producing goods and services. By taking advantage of advanced IT, many companies have taken two steps to reduce costs and improve quality. One is the **empowerment** of their workforces by using powerful new software programs to expand employees' knowledge, tasks, and responsibilities. The other is the creation of **self-managed teams**—groups of employees given responsibility for supervising their own activities and for monitoring the quality of the goods and services they provide.³⁰

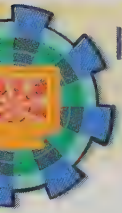
Such teams input the results of their activities into computers, and through IT middle managers have immediate access to what is happening. As a result of IT, members of self-managed teams assume many of the responsibilities and duties previously performed by first-line managers.³¹ What is the role of the first-line manager in this new IT work context? First-line managers act as coaches or mentors whose job is not to tell employees what to do but to provide advice and guidance and help teams find new ways to perform their tasks more efficiently.³² Empire's use of IT to change the tasks and responsibilities of its sales force illustrates many important ways in which IT can affect the management process.

empowerment

The expansion of employees' knowledge, tasks, and responsibilities.

self-managed team

A group of employees who supervises their own activities and monitor the quality of the goods and services they provide.



Information Technology Byte

Empire Insurance Uses CRM to Boost Sales

In 2001, Empire, the largest health insurance provider in New York, sold its health insurance policies through 1,800 sales agents who were responsible for collecting all the customer-specific information needed to determine the price of each customer's insurance policy. Once they had the necessary information, the agents phoned Empire's quotes department, where first-line managers drew up and approved price quotes. These quotes were then relayed to the agents, who in turn relayed them to the customers, who then often modified their requests to lower the cost of the insurance policy. For each modified request, the agent then had to phone the supervisor at Empire again to get a revised price quote. This often happened several times over, with the result that it frequently took over 20 days to close a sale and another 10 days for the customer to get his or her insurance card.

Recognizing that these delays were losing the company sales, Empire's managers decided to examine how a new type of software called *customer relationship management (CRM)* could help improve the sales process. CRM software creates a Web-based IT platform that monitors and controls each of the specific activities involved in selling and delivering products to customers, such as salespeople's

selling activities, product pricing, and after-sales service. CRM software works to integrate all the activities necessary for salespeople in the field to make important decisions and make them quickly.³³

To see if CRM would help improve performance, Empire's managers analyzed all the specific activities involved in their company's sales process. After doing so, they decided to implement a Web-based CRM system that would empower each agent to calculate the insurance quote and offer the customer a binding legal contract. Using the new software, agents themselves now enter all relevant customer data online, and Empire's CRM system generates the quote in a few seconds. Sitting face-to-face with a customer, an agent can continually modify a policy until its price suits the



CRM software improves sales performance by giving salespeople the tools they need to complete customer transactions on the spot.

customer. The sales process that took over 20 days before can now be completed in a few hours using CRM, and customers receive their insurance cards in two to three days.

By promoting the flow of information within the sales function, CRM systems eliminate many problems, such as getting approval for a customer quote and offering a price discount. The role of the first-level manager in the new system is to watch how the now empowered sales agents close sales in order to detect ways to help all agents improve closings.³⁴ Having access to all salespeople's activities, managers, for example, can detect whether a certain selling approach works better than another, determine how much price discount should be offered, and identify changing customer needs so that they can better tailor the product to meet those needs. In essence, Empire's new CRM system not only empowers sales agents but also helps to pinpoint specific ways to improve best sales practices that can be shared across the entire sales force.

John Deere, the well-known manufacturer of tractors, also took steps to empower its employees to raise performance. Deere's managers realized that the employees who assemble its vehicles, with their detailed knowledge about how Deere products work, could become persuasive salespeople. So groups of these employees are now given training in sales techniques and sent to visit Deere customers to explain to them how to operate and service the organization's new products. While speaking with customers, these newly empowered "salespeople" are able to collect information that helps Deere develop new products that appeal to customers. The new sales jobs are temporary. Employees go on assignment but then return to the production line, where they use their new knowledge to find ways to improve efficiency and quality.

Its moves to empower employees have been so successful that Deere negotiated a new agreement with its workers designed to promote empowerment. The agreement specifies that pay increases will be based on workers' learning new skills and completing college courses in areas such as computer programming that will help the company increase efficiency and quality. And the satisfaction that workers feel as they use their new skills and develop new capabilities will increase their commitment to the company and thus help it succeed.

IT and Managerial Roles and Skills

managerial role The set of specific tasks that a manager is expected to perform because of the position he or she holds in an organization.

As the example of Empire suggests, IT is having many important effects on the way managers perform their four functions. IT is also having major effects on the way managers perform their roles and on the skills they develop to perform those roles effectively. A **managerial role** is a set of specific tasks that a manager is expected to perform because of the position he or she holds in an organization. One well-known model of managerial roles was developed by Henry Mintzberg, who detailed 10 specific roles that effective managers undertake. Although Mintzberg's roles overlap with Fayol's model, they are useful because they focus on what managers do in a typical hour, day, or week in an organization as they go about the actual job of managing.³⁵ Below, we discuss these roles and the skills managers need to develop to perform effectively in a time when advanced IT and e-commerce are changing the way managers behave.

Managerial roles identified by Mintzberg

Henry Mintzberg reduced to 10 roles the thousands of specific tasks that managers need to perform as they plan, organize, lead, and control organizational resources.³⁶ Managers assume each of these roles to influence the behavior of individuals and groups inside and outside the organization. People inside the organization include other managers and employees. People outside the organization include shareholders, customers, suppliers, the local community in which an organization is located, and any local or government agency that has an interest in the organization and what it does.³⁷ Mintzberg grouped the 10 roles into three broad categories: *decisional*, *informational*, and *interpersonal*, which are described in Table 1.1. Managers often perform many of these roles from minute to minute while engaged in the more general functions of planning, organizing, leading, and controlling. IT is changing how they do so.

Table 1.1
Managerial Roles Identified by Mintzberg

Type of Role	Specific Role	Examples of Role Activities
Decisional	Entrepreneur	Commit organizational resources to develop innovative goods and services; decide to expand internationally to obtain new customers for the organization's products.
	Disturbance Handler	Move quickly to take corrective action to deal with unexpected problems facing the organization from the external environment, such as a crisis like an oil spill, or from the internal environment, such as producing faulty goods or services.
	Resource Allocator	Allocate organizational resources among different functions and departments of the organization; set budgets and salaries of middle and first-level managers.
	Negotiator	Work with suppliers, distributors, and labor unions to reach agreements about the quality and price of input, technical, and human resources; work with other organizations to establish agreements to pool resources to work on joint projects.
Interpersonal	Figurehead	Outline future organizational goals to employees at company meetings; open a new corporate headquarters building; state the organization's ethical guidelines and the principles of behavior employees are to follow in their dealings with customers and suppliers.
	Leader	Provide an example for employees to follow; give direct commands and orders to subordinates; make decisions concerning the use of human and technical resources; mobilize employee support for specific organizational goals.
	Liaison	Coordinate the work of managers in different departments; establish alliances between different organizations to share resources to produce new goods and services.
Informational	Monitor	Evaluate the performance of managers in different functions and take corrective action to improve their performance; watch for changes occurring in the external and internal environments that may affect the organization in the future.
	Disseminator	Inform employees about changes taking place in the external and internal environments that will affect them and the organization; communicate to employees the organization's vision and purpose.
	Spokesperson	Launch a national advertising campaign to promote new goods and services; give a speech to inform the local community about the organization's future intentions.

DECISIONAL ROLES Decisional roles are closely associated with the methods managers use to plan strategy and utilize resources. IT helps a manager in the role of *entrepreneur* by providing more and better information to use in deciding which projects or programs to initiate and in investing resources to increase organizational performance. As a *disturbance handler*, a manager can get realtime information through IT to manage the unexpected event or crisis that threatens the organization and to implement solutions quickly. As a *resource allocator*, a manager

using human resource software systems from companies such as Oracle and SAP has easy access to the detailed information needed to decide how best to use people and other resources to increase organizational performance. While engaged in that role, the manager must also be a *negotiator*, reaching agreements with other managers or groups claiming the first right to resources or with the organization and outside groups such as suppliers or customers. The emergence of electronic markets and business-to-business (B2B) networks that link organizations to thousands of suppliers is but one example of the many ways IT helps managers perform the negotiator role.

INFORMATIONAL ROLES Informational roles are closely associated with the tasks necessary to obtain and transmit information and so have obviously been dramatically impacted by IT. Acting as a *disseminator*, a manager can use IT to quickly and effectively transmit information to employees to influence their work attitudes and behavior. Wal-Mart, for example, has nationwide videoconferencing linking top managers to each individual store and uses the Internet to provide up-to-date training programs to its employees. IT also provides managers with much greater ability to act as a *spokesperson* and promote the organization so that people inside and outside the organization respond positively to it.

INTERPERSONAL ROLES Managers assume interpersonal roles to provide direction and supervision for both employees and the organization as a whole. IT can make managers much more visible throughout the organization. As a *figurehead*, the person who symbolizes an organization or a department, a CEO can use the Internet to inform employees and other interested parties, such as shareholders, about what the organization's mission is and what it is seeking to achieve. At all levels managers can use email and the Internet to act as figureheads and role models who establish appropriate ways to behave in the organization. For example, anybody in Microsoft is allowed to directly email CEO Bill Gates if he or she thinks it necessary. For similar reasons IT allows managers to perform better as *leaders* because they have more and better-quality information available for training, counseling, and mentoring subordinates to help them reach their full potential. Finally, as a *liaison*, a manager can use IT to improve his or her ability to link and coordinate the activities of people and groups both inside and outside the organization.

Terri Patsos Stanley, the manager of a small short-term rental business, has used IT to help her better perform many of these roles. Patsos Stanley pioneered the concept of providing business travelers with high-quality apartments as an alternative to staying in more expensive and often less convenient hotels in the Boston area. Her company, Boston Short-Term Rentals, grew rapidly because of her drive to keep costs down and customers happy. To achieve these goals, Patsos Stanley had to learn all the different managerial roles.³⁸

As the president of a rapidly growing company, Patsos Stanley is continually required to make decisions. In the role of *entrepreneur*, she searched for opportunities to increase revenues by increasing the number of apartments that she manages. One solution she adopted was to use the Internet and develop a strong presence on the World Wide Web to attract customers. As a *disturbance handler*, she deals with unexpected problems such as plumbing breakdowns in the middle of the night; therefore, all staff members are connected by electronic paging and personal messaging devices to speed response to customer problems. As a *resource allocator*, she decides how much money to spend to refurbish and upgrade the

Ken Chenault, pictured here, is the President and CEO of American Express Company. Promoted in 1997, he climbed the ranks from their Travel Related Services Company, thanks to his "even temper and unrelenting drive." Respected by colleagues for his personality, most will say they can't remember him losing his temper or raising his voice. His open door policy for subordinates allows him to mentor AmEx managers and encourages all to enter and "speak their minds."



apartments to maintain their luxury appeal. She maintains close contact with the apartment owners through the Internet—she sends digital images of the apartments over the Web, for example. As a *negotiator*, she contracts with other organizations such as cleaning or painting services to obtain the most economical services her business requires—once again, the information available through the Internet makes this more efficient.

With more than 200 apartments to oversee, Boston Short-Term Rentals' information management is a vital activity, and Patsos Stanley's role as *monitor* is important. The sophisticated computer system she developed allows her to evaluate the performance of her business by occupancy rates, customer complaints, and other indicators of the quality of her service. The system facilitates her ability to respond quickly to problems as they arise. In her ongoing role as *disseminator*, she uses IT to update her staff with information about changes in visitor arrivals and departures, but as a *spokesperson* she is always on the phone to persuade visitors who may be somewhat hesitant about staying in an apartment that they know nothing about as opposed to staying with a hotel chain that has a well-recognized name.

In fact, Patsos Stanley learned the importance of an extremely hands-on approach to managing her company. She and her employees personally greet the new arrivals and perform the activities that porters, the concierge, and frontdesk staff do in the typical hotel. In interpersonal terms, Patsos Stanley is the *figurehead* who provides the personal touch her guests expect; she is the person they can contact if problems arise. With her small staff of carpenters, electricians, interior decorators, and maintenance workers, she acts as a *leader*, energizing them to provide the quick service that guests expect. She is also a *liaison*, able to link her guests to organizations that provide services they may need, such as dry cleaning, catering, or hairdressing.

Patsos Stanley enjoys the variety of her work and relishes the pleasure of meeting the senior managers, actors, and overseas visitors who stay in the apartments.³⁹

The owner/manager of any small business such as Boston Short-Term Rentals continually performs all these managerial roles.

Being a manager

Our discussion of managerial roles may seem to suggest that a manager's job is highly orchestrated and that management is a logical, orderly process in which managers rationally calculate the best way to use resources to achieve organizational goals. In reality, being a manager often involves acting emotionally and relying on gut feelings. Quick, immediate reactions to situations, rather than deliberate thought and reflection, are an important aspect of managerial action.⁴⁰ Often, managers are overloaded with responsibilities, do not have time to spend on analyzing every nuance of a situation, and therefore make decisions in uncertain conditions without being sure which outcomes will be best.⁴¹ Moreover, for top managers in particular, the current situation is constantly changing, and a decision that seems right today may prove to be wrong tomorrow.

The range of problems that managers face is enormous (*high variety*). Managers frequently must deal with many problems simultaneously (*fragmentation*), often must make snap decisions (*brevity*), and many times must rely on experience gained throughout their careers to do their jobs to the best of their abilities.⁴² It is no small wonder that many managers claim that they are performing their jobs well if they are right just half of the time, and it is understandable why many experienced managers accept failure by their subordinates as a normal part of the learning experience. Managers and their subordinates learn both from their successes and from their failures.

Managerial skills

Both education and experience enable managers to recognize and develop the personal skills they need to put organizational resources to their best use. Michael Dell realized from the start that he lacked sufficient experience and technical expertise in marketing, finance, and planning to guide his company alone. Thus, he recruited experienced managers from other information technology companies, such as IBM and HP, to help him build his company. Research has shown that education and experience help managers acquire three principal types of skills: *conceptual*, *human*, and *technical*.⁴³ As you might expect, the level of these skills that managers need depends on their level in the managerial hierarchy. Typically planning and organizing require higher levels of conceptual skills, while leading and controlling require more human and technical skills.

conceptual skills

The ability to analyze and diagnose a situation and to distinguish between cause and effect.

CONCEPTUAL SKILLS Conceptual skills are demonstrated in the ability to analyze and diagnose a situation and to distinguish between cause and effect. Top managers must possess a high level of conceptual skills because their primary responsibilities are planning and organizing.⁴⁴ By all accounts, Bob Nardelli was appointed as CEO of Home Depot because of his ability to identify new opportunities and mobilize managers and other resources to take advantage of those opportunities.

Formal education and training are very important in helping managers develop conceptual skills. Business training at the undergraduate and graduate (MBA) levels provides many of the conceptual tools (theories and techniques in

marketing, finance, and other areas) that managers need to perform their roles effectively. The study of management helps develop the skills that allow managers to understand the big picture confronting an organization. The ability to focus on the big picture lets managers see beyond the situation immediately at hand and consider choices while keeping in mind the organization's long-term goals.

Today, continuing management education and training, including training in advanced IT, are an integral step in building managerial skills because new theories and techniques are constantly being developed to improve organizational effectiveness, such as B2B networks. A quick scan through a magazine such as *BusinessWeek* or *Fortune* reveals a host of seminars on topics such as advanced marketing, finance, leadership, and human resources management that are offered to managers at many levels in the organization, from the most senior corporate executives to middle managers. Microsoft, IBM, Motorola, and many other organizations designate a portion of each manager's personal budget to be used at the manager's discretion to attend management development programs.

In addition, organizations may wish to develop a particular manager's abilities in a specific skill area—perhaps to learn an advanced component of departmental skills, such as international bond trading, or to learn the skills necessary to implement a new IT system. The organization thus pays for managers to attend specialized programs to develop these skills. Indeed, one signal that a manager is performing well is an organization's willingness to invest in that manager's skill development. Similarly, many nonmanagerial employees who are performing at a high level (because they have studied management) are often sent to intensive management training programs to develop their management skills and to prepare them for promotion to first-level management positions.

human skills The ability to understand, alter, lead, and control the behavior of other individuals and groups.

HUMAN SKILLS Human skills include the ability to understand, alter, lead, and control the behavior of other individuals and groups. The ability to communicate, to coordinate, and to motivate people, and to mold individuals into a cohesive team, distinguishes effective from ineffective managers. By all accounts, Bob Nardelli, Michael Dell, Patricia Russo, and Terri Patsos Stanley all possess a high level of these human skills.

Like conceptual skills, human skills can be learned through education and training, as well as be developed through experience.⁴⁵ Organizations increasingly utilize advanced programs in leadership skills and team leadership as they seek to capitalize on the advantages of self-managed teams.⁴⁶ To manage personal interactions effectively, each person in an organization needs to learn how to empathize with other people—to understand their viewpoints and the problems they face. One way to help managers understand their personal strengths and weaknesses is to have their superiors, peers, and subordinates provide feedback about their performance in the roles identified by Mintzberg. Thorough and direct feedback allows managers to develop their human skills.

technical skills The job-specific knowledge and techniques required to perform an organizational role.

TECHNICAL SKILLS Technical skills are the job-specific knowledge and techniques required to perform an organizational role. Examples include a manager's specific manufacturing, accounting, marketing, and, increasingly, IT skills. Managers need a range of technical skills to be effective. The array of technical skills managers need depends on their positions in their organizations. The manager

of a restaurant, for example, may need cooking skills to fill in for an absent cook, accounting and bookkeeping skills to keep track of receipts and costs and to administer the payroll, and aesthetic skills to keep the restaurant looking attractive for customers.

Effective managers need all three kinds of skills—conceptual, human, and technical. The absence of even one managerial skill can lead to failure. One of the biggest problems that people who start small businesses confront is their lack of appropriate conceptual and human skills. Someone who has the technical skills to start a new business does not necessarily know how to manage the venture successfully. Similarly, one of the biggest problems that scientists or engineers who switch careers from research to management confront is their lack of effective human skills. Management skills, roles, and functions are closely related, and wise managers or prospective managers are constantly in search of the latest educational contributions to help them develop the conceptual, human, and technical skills they need to function in today's changing and increasingly competitive global environment.

competencies The specific set of skills, abilities, and experiences that allows one manager to perform at a higher level than another manager in a particular setting.

Today, the term **competencies** is often used to refer to the specific set of skills, abilities, and experiences that gives one manager the ability to perform at a higher level than another manager in a particular organizational setting. Developing such competencies through education and training has become a major priority for both aspiring managers and the organizations they work for. As we discussed earlier, many people are enrolling in advanced management courses, but many companies, such as General Electric (GE) and IBM, have established their own colleges to train and develop their employees and managers at all levels. Every year, for example, GE puts thousands of its employees through management programs designed to identify the employees who the company believes have superior competencies and whom it can develop to become its future top managers. In many organizations promotion is closely tied to a manager's ability to acquire the competencies that a particular company believes are important.⁴⁷ At 3M, for example, the ability to successfully lead a new product development team is viewed as a vital requirement for promotion; at IBM the ability to attract and retain clients is viewed as a vital competency its consultants must possess. We discuss specific kinds of managerial competencies in most of the chapters of this book. The way in which Steve Jobs learned the skills needed to be an effective manager is discussed in the following case study *Manager as a Person*.



Manager as a Person

Steve Jobs Transforms Apple Computer

In 1976, Steven P. Jobs sold his Volkswagen van, and his partner Steven Wozniak sold his two programmable calculators. They then invested the proceeds of \$1,350 to build a computer circuit board in Jobs's garage. So popular was the circuit board, which was developed into the Apple II personal computer (PC), that in 1977 Jobs and Wozniak incorporated their new business as Apple Computer. By 1985 Apple's sales were almost \$2 billion; nevertheless, in the same year Jobs was forced out of the company he founded. Jobs's approach to management was a big part of the reason he lost control of Apple.⁴⁸



Like many effective managers, Steve Jobs has learned from his mistakes.

After Apple was founded, Steve Jobs saw his role as leading the development effort to create new and improved PCs, and he started many different project teams to develop new and different PC models. Although this was a good strategy, Jobs's management style was often arbitrary and overbearing and caused many problems. He often played favorites among various employees and teams, championing some (e.g., his personal project, the Lisa PC team) against others (the Macintosh team). His actions led to fierce competition among project teams, many misunderstandings, and a great deal of distrust among members of competing teams.⁴⁹

Moreover, Jobs's abrasive management style brought him into conflict with other managers, particularly John Sculley, Apple's CEO. Employees became unsure whether Jobs (the chairman) or Sculley (the CEO) was leading the company, and both managers were so busy competing for control of Apple that neither had the time or energy to ensure that Apple's resources were being used efficiently. For example, little attention was paid to evaluating the performance of the project teams, and there was not even a budget in place to curb the teams' research and development spending. The result? Apple's costs started to soar and its performance and profits fell. Apple's board of directors became convinced that Jobs's management style was the heart of the problem and asked him to resign.

After leaving Apple, Jobs moved on to new ventures. He founded NEXT, which developed a powerful new PC, and Pixar, a computer animation company that became a major success story after it made movies such as *Toy Story* and *Finding Nemo*. In both these companies, Jobs developed a clear vision for managers to follow and built strong management teams. In the meantime, Apple was struggling to compete against Michael Dell's new, low-cost PCs and Microsoft's Windows software.

Apple's performance was declining rapidly, and in 1996 Jobs convinced Apple to buy NEXT for \$400 million and use its powerful operating system in the next generation of Apple PCs. In 1997, Apple asked Jobs to take full control of the company and once again become its CEO.⁵⁰ Jobs agreed and quickly began to put the new management skills he had developed over time to good use. Understanding, more than he had ever before, that what a company needs is clear leadership and a guiding mission to energize and motivate employees, the charismatic Jobs strove to create a new vision for Apple.

Jobs decided that to survive, Apple had to introduce advanced PCs and related equipment. He instituted an across-the-board planning process, established clear company objectives, and created a team structure that allowed programmers and engineers to pool their skills to develop new PCs. He delegated

considerable authority to the teams, but he also established strict timetables and challenging “stretch” goals, such as bringing new products to market as quickly as possible, for these groups to achieve. One result of these efforts was Apple’s sleek new line of iMac PCs, which were quickly followed by a wide range of futuristic PC-related products. To profile the company’s innovations, Jobs opened a nationwide chain of Apple stores.

Jobs’s most recent attempt to revolutionize Apple and raise its performance came in 2003, when he announced that Apple was starting a new service called *iTunes*. Through iTunes, an online music store, people could legally download songs from the Internet by paying a dollar a song. At the same time, Apple introduced its iPod music player, which can store thousands of songs, and the player quickly became a runaway success. In 2004, Apple announced its new mini iPod, which was such a success that retailers could not keep it in stock. By then, Apple had 70 percent of the online music download business!⁵¹

In 2005, it seemed that a new Apple was emerging. Analysts credit Apple’s rising performance to the management skills Jobs was forced to develop after his ouster from the company he had founded. However, with Dell the acknowledged low-cost PC maker, will Apple’s new venture into the music business be enough to guarantee its future success?

Challenges for Management in a Global Environment

global organizations

Organizations that
operate and compete in
more than one country.

Because the world has been changing more rapidly than ever before, managers and other employees throughout an organization must perform at higher and higher levels.⁵² In the last 20 years, competition between organizations competing domestically (in the same country) and globally (in countries abroad) has increased dramatically. The rise of **global organizations**, organizations that operate and compete in more than one country, have put severe pressure on many other organizations to improve their performance and to identify better ways to use their resources. The successes of the German chemical companies Schering and Hoechst, Italian furniture manufacturer Natuzzi, Korean electronics companies Samsung and LG, Brazilian plane maker Embraer, and Europe’s Airbus Industries are putting pressure on organizations in other countries to raise their level of performance to compete successfully with these global companies.

Even in the not-for-profit sector, global competition is spurring change. Schools, universities, police forces, and government agencies are reexamining their operations because of looking at the way things are done in other countries. For example, many curriculum and teaching changes in the United States have resulted from the study of methods that Japanese and European school systems use. Similarly, European and Asian hospital systems have learned much from the U.S. system—which may be the most effective, though not the most efficient, in the world.

Today, managers who make no attempt to learn and adapt to changes in the global environment find themselves reacting rather than innovating, and their organizations often become uncompetitive and fail.⁵³ Four major challenges stand out for managers in today’s world: building a competitive advantage, maintaining ethical standards, managing a diverse workforce, and utilizing new information systems and technologies.

Building competitive advantage

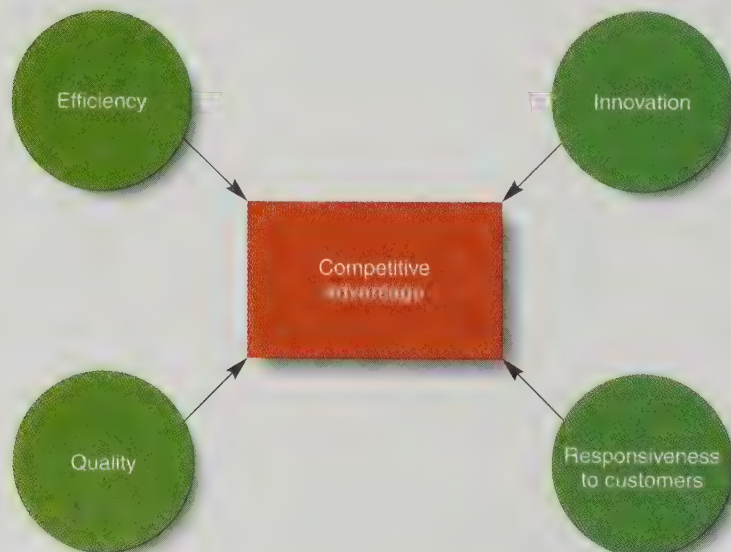
competitive advantage The ability of one organization to outperform other organizations because it produces desired goods or services more efficiently and effectively than its competitors.

What are the most important lessons for managers and organizations to learn if they are to reach and remain at the top of the competitive environment of business? The answer relates to the use of organizational resources to build a competitive advantage. **Competitive advantage** is the ability of one organization to outperform other organizations because it produces desired goods or services more efficiently and effectively than its competitors. The four building blocks of competitive advantage are superior *efficiency*; *quality*; *speed*, *flexibility*, and *innovation*; and *responsiveness to customers* (see Figure 1.5).

INCREASING EFFICIENCY Organizations increase their efficiency when they reduce the quantity of resources (such as people and raw materials) they use to produce goods or services. In today's competitive environment, organizations constantly are seeking new ways to use their resources to improve efficiency. Many organizations are training their workforces in the new skills and techniques needed to operate heavily computerized assembly plants. Similarly, cross-training gives employees the range of skills they need to perform many different tasks, and to organize employees in new ways, such as in self-managed teams, allowing them to make good use of their skills. These are important steps in the effort to improve productivity. Japanese and German companies invest far more in training employees than do American or Italian companies.

Managers must improve efficiency if their organizations are to compete successfully with companies operating in Mexico, Malaysia, and other countries where employees are paid comparatively low wages. New methods must be devised either to increase efficiency or to gain some other competitive advantage—higher-quality goods, for example—if outsourcing and the loss of jobs to low-cost countries are to be prevented.

Figure 1.5
Building Blocks
of Competitive
Advantage



INCREASING QUALITY The challenge from global organizations such as Korean electronics manufacturers, Mexican agricultural producers, and European marketing and financial firms also has increased pressure on companies to improve the skills and abilities of their workforces in order to improve the quality of their goods and services. One major thrust to improving quality has been to introduce the quality-enhancing techniques known as *total quality management (TQM)*. Employees involved in TQM are often organized into quality control teams and are responsible for continually finding new and better ways to perform their jobs; they also must monitor and evaluate the quality of the goods they produce. TQM is based on a significant new philosophy of managing behavior in organizations; we thoroughly discuss this approach and ways of managing TQM successfully in Chapter 14.

INCREASING SPEED, FLEXIBILITY, AND INNOVATION Today, companies can win or lose the competitive race depending on their speed—how fast they can bring new products to market—or their flexibility—how easily they can change or alter the way they perform their activities to respond to the actions of their competitors. Companies that have speed and flexibility are agile competitors: Their managers have superior planning and organizing abilities; they can think ahead, decide what to do, and then speedily mobilize their resources to respond to a changing environment. We examine how managers can build speed and flexibility in their organizations in later chapters. Steve Jobs's goal is to make Apple an agile company that can react to the continuous changes taking place in computing and digital entertainment so that it can build a competitive advantage.

Innovation, the process of creating new or improved goods and services that customers want or developing better ways to produce or provide goods and services, poses a special challenge. Managers must create an organizational setting in which people are encouraged to be innovative. Typically, innovation takes place in small groups or teams; management decentralizes control of work activities to team members and creates an organizational culture that rewards risk taking. Understanding and managing innovation and creating a work setting that encourages risk taking are among the most difficult managerial tasks.

INCREASING RESPONSIVENESS TO CUSTOMERS Organizations compete for customers with their products and services, so training employees to be responsive to customers' needs is vital for all organizations, but particularly for service organizations. Retail stores, banks, and hospitals, for example, depend entirely on their employees to perform behaviors that result in high-quality service at a reasonable cost.⁵⁴ As many countries (the United States, Canada, and Great Britain are just a few) move toward a more service-based economy (in part because of the loss of manufacturing jobs to China, Malaysia, and other countries with low labor costs), managing behavior in service organizations is becoming increasingly important. Many organizations are empowering their customer service employees and giving them the authority to take the lead in providing high-quality customer service. As noted previously, the empowering of nonmanagerial employees changes the role of first-line managers and often leads to the more efficient use of organizational resources.

Achieving a competitive advantage requires that managers use all their skills and expertise to develop resources and improve efficiency, quality, innovation, and responsiveness to customers. We revisit this theme often as we examine the ways managers plan strategies, organize resources and activities, and lead and control

people and groups to effectively use human and other resources to achieve organizational goals.

Maintaining ethical and socially responsible standards

While mobilizing organizational resources, managers at all levels are under considerable pressure to increase the level at which their organizations perform.⁵⁵ For example, top managers receive pressure from shareholders to increase the performance of the entire organization to boost the stock price, improve profits, or raise dividends. In turn, top managers may then pressure middle managers to find new ways to use organizational resources to increase efficiency or quality and thus attract new customers and earn more revenues.

Pressure to increase performance can be healthy for an organization because it causes managers to question the way the organization is working and it encourages them to find new and better ways to plan, organize, lead, and control. However, too much pressure to perform can be harmful.⁵⁶ It may induce managers to behave unethically in dealings with individuals and groups both inside and outside the organization.⁵⁷ For example, a purchasing manager for a large retail chain might buy inferior clothing as a cost-cutting measure; or to secure a large foreign contract, a sales manager in a large defense company might offer bribes to foreign officials. In 2004, the four top executives of Lucent's Korean division were fired after it was revealed they used bribery to obtain lucrative contracts for Lucent in that country.⁵⁸ The issue of social responsibility concerns the obligations that a company should have toward people and groups such as customers or the communities in which they operate. An example of companies that act in a socially irresponsible and unethical way is described in the following "Ethics in Action."



Ethics in Action

Diet Supplement Makers and the FDA

On April 12, 2004, it became illegal to make or sell the dietary supplement ephedra in the United States.⁵⁹ The Food and Drug Administration (FDA) had finally obtained information from users and from makers of ephedra pills, such as Yellow Jackets and Black Beauties, that revealed over 16,000 adverse-report events experienced by users of the drug. At least 36 deaths were directly related to the use of the drug, including the death of Baltimore Oriole pitcher Steven Bechler in 2003.

Ephedra has been widely available for a decade; why did it take the FDA so long to ban the use of the drug? Diet supplement makers, unlike major pharmaceutical companies, have been shielded by a 1994 law. The law does not require that the makers of dietary supplements report adverse incidents to the FDA, but it obligates the FDA to prove unreasonable public health risks.

To protect their businesses, ephedra makers like Metabolife and NVE Pharmaceuticals did not reveal complaints about their products—from thousands of customers—until forced to do so by lawsuits brought by people harmed by the


drug. In 2003 Metabolife finally released over 16,000 customer reports about its ephedra products that listed nearly 2,000 adverse reactions, including 3 deaths, 20 heart attacks, 24 strokes, and 40 seizures.⁶⁰ Robert Occhifinto, a twice-convicted felon and the owner of NVE, with annual revenues of \$80 million from sales of ephedra-based supplements, faces at least 30 product liability lawsuits.⁶¹

In their attempts to protect the \$18 billion-a-year dietary supplement business, makers of dangerous drugs like ephedra continue to behave in unethical and socially irresponsible ways. In particular, they have begun to use other chemical compounds that have ephedra-like effects in new varieties of pills. In 2004, the FDA issued warnings on eight types of chemical compounds about which it is receiving many reports of adverse reactions and advised consumers not to use supplements containing these compounds.⁶² In view of the fact that dietary supplement makers are making no attempts to ensure the safety of their products, the push is on for Congress to pass regulations that will subject these companies to the same kind of scrutiny and reporting requirements as those governing pharmaceutical companies.

Managing a diverse workforce

Another challenge for managers is to recognize the need to treat human resources in a fair and equitable manner. Today, the age, gender, race, ethnicity, religion, sexual preference, and socioeconomic makeup of the workforce present new challenges for managers. Managers must establish employment procedures and practices that are legal, are fair, and do not discriminate against any organizational members.⁶³

In the past, white male employees dominated the ranks of management. Today increasing numbers of organizations are realizing that to motivate effectively and take advantage of the talents of a diverse workforce, they must make promotion opportunities available to all employees, including women and minorities.⁶⁴ Managers must also recognize the performance-enhancing possibilities of a diverse workforce, such as the ability to take advantage of the skills and experiences of different kinds of people.⁶⁵ The following “Focus on Diversity” feature looks at how one company took advantage of diversity to enhance its competitive advantage.



Focus on Diversity

How Diversity Can Promote Competitive Advantage

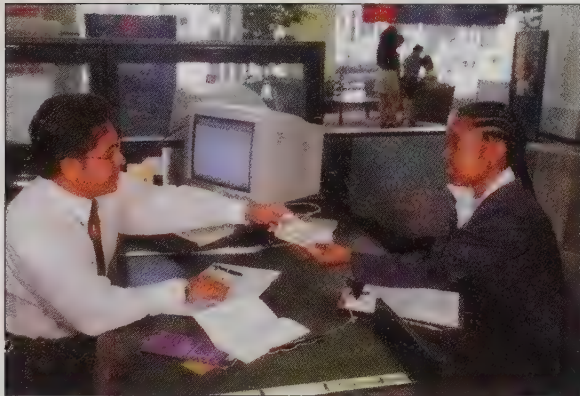
With assets of over \$40 billion in 2005, Union Bank of California, based in San Francisco, is among the 30 largest banks in the United States.⁶⁶ It has enjoyed great success and growth throughout the last decade, in large part because of the approach it has developed to diversity—an approach that reflects the needs of its employees, customers, and environment. Indeed, from 1999 to 2005 the company has been listed among *Fortune* magazine’s 50 best companies for minorities

to work for, and its diversity practices have become a model for many other companies seeking to emulate its success.⁶⁷

Union Bank operates in one of the most diverse states in the nation, California, where more than half the population is Asian, Black, Hispanic, or gay. Recognizing this fact, the bank always had a policy of hiring and recruiting diverse employees. However, not until 1996 did the bank realize that the diversity of its employees created a competitive advantage. In that year, George Ramirez, a vice president at Union Bank, suggested that the bank create a marketing group to develop a plan for attracting customers who were Hispanic, like himself. So successful was this venture that a group of African-American employees created a marketing group to develop a campaign aimed at attracting new African-American customers, and later Asian-American and gay and lesbian employees did the same. After these groups' considerable success in recruiting new customers, it was clear to Union Bank's managers that they should use employee diversity as a way of improving customer service. For example, when customers walk into a bank branch in a predominantly Latino neighborhood, they are now greeted by substantial numbers of Latino employees.⁶⁸

The bank, like many other organizations, also discovered that diversity can lead to competitive advantage because diverse employees approach the same issue—for example, how to attract customers—in very different ways. The bank

found that creating diverse teams of employees helped improve the quality of decision making inside the organization.⁶⁹ Furthermore, the bank's reputation of being a good place for minorities to work attracted highly skilled and motivated minority job candidates. As its former CEO Takahiro Moriguchi said when accepting a national diversity award for the company, "By searching for talent from among the disabled, both genders, veterans, all ethnic groups and all nationalities, we gain access to a pool of ideas, energy, and creativity as wide and varied as the human race itself. I expect diversity will become even more important as the world gradually becomes a truly global marketplace."⁷⁰



Union Bank's customer service representatives, such as the employee pictured here, are well known for building relationships with their diverse customer groups to improve the level of customer service. The diverse nature of Union Bank's employees reflects the diverse customer groups the bank serves.

Managers who value their diverse employees not only invest in developing these employees' skills and capabilities but also link rewards to their performance. They are the managers who best succeed in promoting performance over the long run.⁷¹ Today, more and more organizations are realizing that people are their most important resource and that developing and protecting human resources is an important challenge for management in a competitive global environment. We discuss the many issues surrounding the management of a diverse workforce in Chapter 3.

Utilizing IT and e-commerce

As has already been discussed, another important challenge for managers is the efficient utilization of new information technology and e-commerce.⁷² New technologies such as computer-controlled manufacturing and information systems that link and enable employees in new ways are continually being developed. In a setting that uses self-managed teams, for example, sophisticated computer information systems link the activities of team members so that each member knows what the others are doing. This coordination helps to improve quality and increase the pace of innovation. Microsoft, Hitachi, IBM, and other companies make extensive use of information systems such as email, the Internet, and videoconferencing, accessible by means of PCs, to build a competitive advantage. The importance of IT is discussed in detail in Chapter 13 and throughout the text you will find icons that alert you to examples of how IT is changing the way companies operate.

Summary and Review

WHAT IS MANAGEMENT? A manager is a person responsible for supervising the use of an organization's resources to meet its goals. An organization is a collection of people who work together and coordinate their actions

to achieve a wide variety of goals. Management is the process of using organizational resources to achieve organizational goals effectively and efficiently through planning, organizing, leading, and controlling. An efficient organization makes the most productive use of its resources. An effective organization pursues appropriate goals and achieves these goals by using its resources to create the goods or services that customers want.

MANAGERIAL FUNCTIONS The four principal managerial functions are planning, organizing, leading, and controlling. Managers at all levels of the organization and in all departments perform these functions. Effective management means managing these activities successfully.

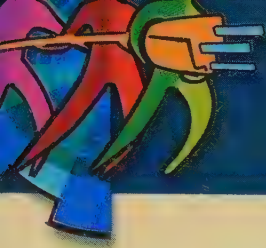
TYPES OF MANAGERS Organizations typically have three levels of management. First-line managers are responsible for the day-to-day supervision of nonmanagerial employees. Middle managers are responsible for developing and utilizing organizational resources efficiently and effectively. Top managers have cross-departmental responsibility. The top manager's job is to establish appropriate goals for the entire organization and to verify that department managers are utilizing resources to achieve those goals. To increase efficiency and effectiveness, some organizations have altered their managerial hierarchies by restructuring, empowering their workforces, utilizing self-managed teams, and utilizing new information technology.

IT AND MANAGERIAL ROLES AND SKILLS According to Mintzberg, managers play 10 different roles: figurehead, leader, liaison, monitor, disseminator, spokesperson, entrepreneur, disturbance handler, resource allocator, and negotiator. Three types of skills help managers perform these roles effectively:

conceptual, human, and technical skills. IT is changing both the way managers perform their roles and the skills they need to perform these roles because it provides richer and more meaningful information.

CHALLENGES FOR MANAGEMENT IN A GLOBAL ENVIRONMENT

Today's competitive global environment presents many interesting challenges to managers. One of the main challenges is building a competitive advantage by increasing efficiency; quality; speed, flexibility, and innovation; and customer responsiveness. Other challenges are behaving ethically toward people inside and outside the organization, managing a diverse workforce, and utilizing new information systems and technologies.



Management in Action

Topics for Discussion and Action

Discussion

1. Describe the difference between efficiency and effectiveness, and identify real organizations that you think are, or are not, efficient and effective.
2. In what ways can managers at each of the three levels of management contribute to organizational efficiency and effectiveness?
3. Identify an organization that you believe is high-performing and one that you believe is low-performing. Give 10 reasons why you think the performance levels of the two organizations differ so much.

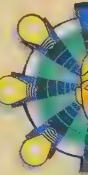
4. What are the building blocks of competitive advantage? Why is obtaining a competitive advantage important to managers?
5. In what ways do you think managers' jobs have changed the most over the last 10 years? Why have these changes occurred?

Action

6. Choose an organization such as a school or a bank; visit it; then list the different organizational resources it uses.
7. Visit an organization, and talk to first-line, middle, and top managers about their

respective management roles in the organization and what they do to help the organization be efficient and effective.

8. Ask a middle or top manager, perhaps someone you already know, to give examples of how he or she performs the managerial functions of planning, organizing, leading, and controlling. How much time does he or she spend in performing each function?
9. Like Mintzberg, try to find a cooperative manager who will allow you to follow him or her around for a day. List the roles the manager plays, and indicate how much time he or she spends performing them.



Building Management Skills

Thinking About Managers and Management

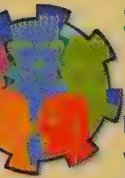
Think of an organization that has provided you with work experience and of the manager to whom you reported (or talk to someone who has had extensive work experience); then answer these questions.

1. Think of your direct supervisor. Of what department is he or she a member, and at what level of management is this person?
2. How do you characterize your supervisor's approach to management? For example, which particular management functions and roles does this person perform most often? What kinds of management skills does this manager have?
3. Do you think the functions, roles, and skills of your supervisor are appropriate for the particular job he or she performs? How could this manager improve his or her task performance? How can IT affect this?
4. How did your supervisor's approach to management affect your attitudes and behavior? For example, how well did you perform as a subordinate, and how motivated were you?
5. Think of the organization and its resources. Do its managers utilize organizational resources effectively? Which resources contribute most to the organization's performance?
6. Describe the way the organization treats its human resources. How does this treatment affect the attitudes and behaviors of the workforce?

7. If you could give your manager one piece of advice or change one management practice in the organization, what would it be?

8. How attuned are the managers in the organization to the need to increase efficiency, quality, innovation, or responsiveness to customers? How well do you

think the organization performs its prime goals of providing the goods or services that customers want or need the most?



Small Group Breakout Exercise

Opening a New Restaurant

Form groups of three or four people, and appoint one group member as the spokesperson who will communicate your findings to the entire class when called on by the instructor. Then discuss the following scenario.

You and your partners have decided to open a large, full-service restaurant in your local community; it will be open from 7 A.M. to 10 P.M. to serve breakfast, lunch, and dinner. Each of you is investing \$50,000 in the venture, and together you have secured a bank loan for an additional \$300,000 to begin operations. You and your partners have little experience in managing a restaurant beyond serving meals or eating in restaurants, and you now face the task of deciding how you will manage the

restaurant and what your respective roles will be.

1. Decide each partner's managerial role in the restaurant. For example, who will be responsible for the necessary departments and specific activities? Describe your managerial hierarchy.
2. Which building blocks of competitive advantage do you need to establish to help your restaurant succeed? What criteria will you use to evaluate how successfully

you are managing the restaurant?

3. Discuss the most important decisions that must be made about (a) planning, (b) organizing, (c) leading, and (d) controlling to allow you and your partners to utilize organizational resources effectively and build a competitive advantage.
4. For each managerial function, list the issue that will contribute the most to your restaurant's success.



Be the Manager

Problems at Achieva

You have just been called in to help managers at Achieva, a fast-growing Internet software company that specializes in B2B network software. Your job is to help Achieva solve some management problems that have arisen because of its rapid growth.

Customer demand to license Achieva's software has boomed so much in just two years that more than 50 new software programmers have been added to help develop a new range of software products. Achieva's growth has been so swift

that the company still operates informally, its organizational structure is loose and flexible, and programmers are encouraged to find solutions to problems as they go along. Although this structure worked well in the past, you have been told that problems are arising.

Increasingly employees have complained that good performance is not being recognized in the organization and that they do not feel equitably treated. Moreover, employees have complained about getting managers to listen to their new ideas and to act on them. A

bad atmosphere is developing in the company, and recently several talented employees have left. Your job is to help Achieva's managers solve these problems quickly and keep the company on the fast track.

Questions

1. What kinds of organizing and controlling problems is Achieva suffering from?
2. What kinds of management changes need to be made to solve them?

Additional Activities on the Build Your Management Skills DVD

- **Test Your Knowledge:**
 - (1) Managerial Functions
 - (2) Categories of Managerial Control, and (3) Management's Historical Figures
- **Self-Assessment:** Career Planning Based on Brain Dominance and Thinking Styles Inventory
- **Manager's Hot Seat:**
 - (1) Project Management: Steering the Committee and
 - (2) Management's Historical Figures

Managing Ethically

Think about an example of unethical behavior that you observed in the past. The incident could be something you experienced as an employee or a customer or something you observed informally.

1. Either by yourself or in a group, give three reasons why you think the behavior was unethical. For example, what rules or norms were broken? Who benefited or was harmed by what took place? What was the outcome for the people involved?
2. What steps might you take to prevent such unethical behavior and encourage people to behave in an ethical way?

BusinessWeek

Case in the News

The Hard Work in Leadership

W. James McNerney, Jr., has been running big outfits for a dozen years now, at General Electric (GE) and, since January 1, 2001, as chairman and chief executive of 3M. Success at these giants means more than drafting smart business plans, of course. It means getting tens of thousands of people to do what you want. But as the financial numbers at GE and 3M show, McNerney can do it.

His secret? Part of it is simply personality and upbringing: His father, Walter, instilled in him a sense of modesty and a drive to always do better, as well as passing along his own sharp intellect. Part of it is practice: McNerney has been a leader since his days at New Trier High School in Winnetka, Illinois, as president of the Tri-Ship boys club in 1966–67 and pitcher on the varsity baseball team. Another part of it is the tutelage he received during

his 18 years at GE, working for now-retired Chairman and CEO Jack Welch.

Recently, McNerney sat down in his 14th-floor suite at 3M headquarters in St. Paul, Minnesota, with *BusinessWeek* Senior Correspondent Michael Arndt. The first outsider ever to become CEO at 3M, McNerney is notoriously press shy. Yet, when it comes to management, he's voluble, talking at length on everything from motivation and corporate culture to the uses of statistical gauges like Six Sigma in personnel screening and his own style as a boss. Edited excerpts of their conversation follow:

Q: I was here two years ago, when you were still pretty new, so I'd like to start by asking you how you think you've done since then.

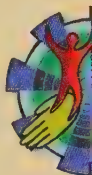
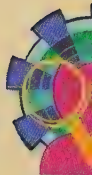
A: The best measurement of progress is the engagement of the

organization, the enthusiasm of the organization: Are we more one team focused on similar things, pulling together? And I feel pretty good about that.

The initiatives I talked about two years ago are exactly the same ones we have today. I believe in boring consistency of meaningful themes. Don't change the message. That's important when you're leading a big organization. Otherwise, people are waiting for the *initiative du jour*. The challenge for us is to keep refreshing them and making them meaningful.

Q: How do you achieve that team spirit?

A: My experience is that if people are convinced they're growing as they pursue company goals, that's when you get ignition. I'll use Six Sigma as an example. People are learning new ways to approach



business problems, new ways to lead other people. They're achieving results that are better than what they had achieved before, so they feel they are becoming better managers.

I think when everybody does that, we become a better company. When people's growth lines up with corporate growth, that's when you get the motivation, the enthusiasm, the alignment that every CEO hopes for. The trick is to find these things.

Q: A lot of CEOs have these goals, but how do you actually get this accomplished?

A: It comes down to personal engagement. I spend a lot of time out with our people. Let me give you an example of this: leadership development. We need to get the middle of this company moving and growing and aspiring to be tomorrow's leaders. It's easy to make the speech about leadership and then disappear into a backroom grading everybody.

That's one approach. Another is what we try to do. We spent a year debating what leadership is. I made speeches on the subject and solicited input from everybody. So when we hammered it out, it was the company's leadership goals we were aspiring to—not the CEO's, not some consultant's, not what we read in a book last week. So now the organization is quite happy to be measured and to aspire to these things because they created them.

Now we could have done this Day One, but I learned over the years that to short-circuit that process is very risky for a guy running an organization. Most CEOs—and I don't want to preach here—are smart enough to figure out where to go with a company. The hard work is engaging everyone in doing it. That's the hard work in leadership.

Q: Looking at your typical work-day, how do you spend your time? Is most of it spent on managing people? Or thinking up grand strategies? Or scrutinizing the company's numbers?

A: Designing business strategy is probably what I spend the least amount of time on. I rely on our business leadership to do a lot of that. I spend more time on people issues broadly defined: Who's in what job? How do we accelerate this career? What programs do we have in place to train people? How do we make people fit better? How do we pay them? How do you differentiate pay?

I also spend a lot of time on communication, broadly defined. I probably do 30 major events a year with 100 people or more, where I spend time debating things and pushing my ideas, telling them what I'm thinking that day and soliciting feedback. What is it we're doing? And why?

I want a lot of feedback on how to run this company. The trick for me is to create an environment where I get honest feedback. That's the hard part. The natural tendency for people is to say, Jim, what a great idea!

Q: Do you think you've got to the stage where you're getting honest feedback?

A: In some cases, but not always. It's hard for people to have self-confidence and say they disagree. 3M was a pretty hierarchical place with not a lot of free-form discussion. I think we've made a lot of progress there. But these changes don't happen overnight.

Q: You've been here since 2001. What surprised you in being difficult?

A: I think the whole issue of leadership development. I think we've made enormous progress, but I'm still impressed with how much farther

we have to go. I wouldn't characterize it as a disappointment. I would say that where I'm going to be in two years, I wished I was there now.

3M is a business with a big brand and a big global stance and can be a bigger company. We have to keep growing big leaders. We've accelerated some careers. But we also have highly valued people who have been in jobs a while. You can't just throw people out. There's the balance between the young and energized and the experienced and effective. We're constantly wrestling with that.

Q: Let me ask you the corollary question: Are there things that you had expected to be real challenges when you came to 3M that turned out to be a snap?

A: The big surprise for me was how open 3M-ers were to change. I thought there would be more resistance to a new way of doing things, a new language, a new CEO. But I found a company who thought they weren't achieving all they could, and they were willing to team up with somebody to do more. That was a surprise.

Q: What skills and attributes that you developed at GE transferred easily here?

A: I think the thing that helped me the most was, at GE you run so many different businesses. I was changing jobs every two or three years, and each one of those businesses had very different cultures and different geographies and different values. So coming here and trying to force this alliance was something I had done three or four times before.

Q: It seems to me from what I'm hearing that you do a lot by encouraging people.

A: It's the balance between setting expectations and encouraging. I

think the harder you push people, the more you have to encourage them.

Some people feel you either have a demanding, command-and-control management style or you have a nurturing, encouraging management style. I believe you have to have both. If you're only demanding, without encouraging, eventually that runs out of gas. And if

you're only encouraging without setting high expectations, you're not getting as much out of people. It's not either/or. You can't have one without the other.

Questions

1. What is James McNerney's approach to managing?

2. What kind of skills and abilities does McNerney possess that led him to become 3M's CEO?

Source: Michael Arndt, "The Hard Work in Leadership." Reprinted from the April 12, 2004, issue of *BusinessWeek* by special permission. Copyright © by the McGraw-Hill Companies, Inc.

BusinessWeek

Case in the News

Can a U.S.-Style Boss Rev Up Siemens?

It's safe to say Klaus Kleinfeld didn't have much trouble adjusting to life in America after Siemens made him chief operating officer of its U.S. unit in 2001. Kleinfeld soon won invitations to join the boards of a dozen prestigious organizations including the Metropolitan Opera and Alcoa Inc. He ran two New York marathons and frequented the city's jazz clubs. Under Kleinfeld, who was promoted to CEO of Siemens' U.S. unit in 2002, the company played a big role in building Houston's Reliant Stadium, scene in 2004 of that most American of events, the Super Bowl.

Now, Kleinfeld, 46, is set to become the latest German manager to parlay U.S. experience and attitude into a top job at a German corporate icon. On July 7, 2004, Siemens announced that, effective in January, Kleinfeld will succeed Heinrich von Pierer as CEO of the \$89 billion Munich conglomerate, which makes everything from light bulbs and power plants to trains and mobile phones. The question is whether the energetic Kleinfeld will

fare better than some other German bosses who tried to import U.S.-style management techniques, with their emphasis on speed and profit. "Kleinfeld stands for the modern approach in German industry, of trying to cope with globalization and move out of the old, well-trodden path," says Jens van Scherpenberg, head of the Americas Research Unit at the German Institute for International & Security Affairs, a Berlin think tank.

The Right Stuff?

The CEO-designate has already begun to make changes. His fingerprints were on Siemens' decision, also announced on July 7, 2004, to merge the mobile phone division with the land-line telecom unit. In the United States, Kleinfeld managed to get Siemens' disparate fiefdoms to cooperate more on marketing. One result was the contract to provide everything from telecom equipment to computer networks for Houston's \$750 million Reliant Park convention and sporting complex.

In fact, Kleinfeld probably won the top job because he showed he could get Siemens divisions to work together to win big orders. The company has struggled for years to prove that synergies among branches justify the inherent unwieldiness of a far-flung conglomerate. He also got Siemens' legions of proud engineers to see things more from their customers' point of view. After a \$553 million loss in 2001, Siemens reported an \$810 million profit for its U.S. units in 2002 and a \$561 million profit in 2003, after which Kleinfeld returned to Germany. "He was instrumental in getting it working," says Gerhard Schulmeyer, Kleinfeld's predecessor as CEO of Siemens in the U.S.

Back home, Kleinfeld will have to spend a lot of time smoothing out relations with politicians and unions. In the United States, where Siemens had sales of \$16.6 billion in 2003, the company cut staff by 15,000 to 65,000, by selling or closing unprofitable units, but also by shifting work to lower-wage countries such as India. Von Pierer has

reduced the German workforce by more than 50,000, to 167,000, since becoming CEO in 1992.

But by imposing cuts gradually, the diplomatic von Pierer managed to avoid serious confrontation with Germany's powerful labor unions and their allies in Parliament. That is becoming more difficult. Labor leaders are sore that they were forced recently to give in to demands that workers at a mobile phone factory put in extra hours without extra pay: Siemens threatened to shift the work to Hungary. "Siemens has damaged its image with that kind of action," says

Wolfgang Müller, a worker on the supervisory board.

Kleinfeld will have to do a lot of creative thinking. But people who have worked with him say he's good at that. "He was exceptionally exact but not narrow-minded; on the contrary, very independent and creative," says Peter Fassheber, a retired professor at Georg-August University in Göttingen who supervised Kleinfeld's research in the early 1980s. Kleinfeld focused on the intersection of psychology and economics. If Kleinfeld can reconcile human nature with economic reality at Siemens, he might just succeed.

Questions

1. How would you describe Klaus Kleinfeld's approach to managing?
2. What skills and abilities helped him rise to become Seimen's CEO?

Source: Jack Ewing, "Can a U.S.-Style Boss Rev Up Siemen?" Reprinted from the July 26, 2004, issue of *BusinessWeek* by special permission. Copyright © 2004 by the McGraw-Hill Companies, Inc.

History of Management Thought

APPENDIX

A

The systematic study of management began in the closing decades of the nineteenth century, after the Industrial Revolution had swept through Europe and America. In the new economic climate, managers of all types of organizations—political, educational, and economic—were increasingly turning their focus toward finding better ways to satisfy customers' needs. Many major economic, technical, and cultural changes were taking place at this time. With the introduction of steam power and the development of sophisticated machinery and equipment, the Industrial Revolution changed the way goods were produced, particularly in the weaving and clothing industries. Small workshops run by skilled workers who produced hand-manufactured products (a system called *crafts production*) were being replaced by large factories in which sophisticated machines controlled by hundreds or even thousands of unskilled or semiskilled workers made products. For example, raw cotton and wool that in the past families or whole villages working together had spun into yarn were now shipped to factories where workers operated machines that spun and wove large quantities of yarn into cloth.

Owners and managers of the new factories found themselves unprepared for the challenges accompanying the change from small-scale crafts production to large-scale mechanized manufacturing. Moreover, many of the managers and supervisors in these workshops and factories were engineers who had only a technical orientation. They were unprepared for the social problems that occur when people work together in large groups (as in a factory or shop system). Managers began to search for new techniques to manage their organizations' resources, and soon they began to focus on ways to increase the efficiency of the worker–task mix. They found help from Frederick W. Taylor.

F. W. Taylor and Scientific Management

Frederick W. Taylor (1856–1915) is best known for defining the techniques of **scientific management**, the systematic study of relationships between people and tasks for the purpose of redesigning the work process to increase efficiency. Taylor was a manufacturing manager who eventually became a consultant and taught other managers how to apply his scientific management techniques. Taylor believed that if the amount of time and effort that each worker expends to produce a unit of output (a finished good or service) can be reduced by increasing specialization and the division of labor, the production process will become more efficient. Taylor believed the way to



Frederick W. Taylor, founder of Scientific Management, and one of the first people to study the behavior and performance of people at work.

create the most efficient division of labor could best be determined by using scientific management techniques, rather than intuitive or informal rule-of-thumb knowledge. Based on his experiments and observations as a manufacturing manager in a variety of settings, he developed four principles to increase efficiency in the workplace:¹

- Principle 1: *Study the way workers perform their tasks, gather all the informal job knowledge that workers possess, and experiment with ways of improving the way tasks are performed.*

To discover the most efficient method of performing specific tasks, Taylor studied in great detail and measured the ways different workers went about performing their tasks. One of the main tools he used was a time and motion study, which involves the careful timing and recording of the actions taken to perform a particular task. Once Taylor understood the existing method of performing a task, he then experimented to increase specialization; he tried different methods of dividing up and coordinating the various tasks necessary to produce a finished product. Usually this meant simplifying jobs and having each worker perform fewer, more routine tasks. Taylor also sought to

find ways to improve each worker's ability to perform a particular task—for example, by reducing the number of motions workers made to complete the task, by changing the layout of the work area or the type of tool workers used, or by experimenting with tools of different sizes.

- Principle 2: *Codify the new methods of performing tasks into written rules and standard operating procedures.*

Once the best method of performing a particular task was determined, Taylor specified that it should be recorded so that the procedures could be taught to all workers performing the same task. These rules could be used to further standardize and simplify jobs—essentially, to make jobs even more routine. In this way efficiency could be increased throughout an organization.

- Principle 3: *Carefully select workers so that they possess skills and abilities that match the needs of the task, and train them to perform the task according to the established rules and procedures.*

To increase specialization, Taylor believed workers had to understand the tasks that were required and be thoroughly trained in order to perform a task at the required level. Workers who could not be trained to this level were to be transferred to a job where they were able to reach the minimum required level of proficiency.²

- Principle 4: *Establish a fair or acceptable level of performance for a task, and then develop a pay system that provides a reward for performance above the acceptable level.*

To encourage workers to perform at a high level of efficiency, and to provide them with an incentive to reveal the most efficient techniques for performing a task, Taylor advocated that workers benefit from any gains

in performance. They should be paid a bonus and receive some percentage of the performance gains achieved through the more efficient work process.

By 1910, Taylor's system of scientific management had become nationally known and in many instances faithfully and fully practiced.³ However, managers in many organizations chose to implement the new principles of scientific management selectively. This decision ultimately resulted in problems. For example, some managers using scientific management obtained increases in performance, but rather than sharing performance gains with workers through bonuses as Taylor had advocated, they simply increased the amount of work that each worker was expected to do. Many workers experiencing the reorganized work system found that as their performance increased, managers required them to do more work for the same pay. Workers also learned that increases in performance often meant fewer jobs and a greater threat of layoffs, because fewer workers were needed. In addition, the specialized, simplified jobs were often monotonous and repetitive, and many workers became dissatisfied with their jobs.

From a performance perspective, the combination of the two management practices—(1) achieving the right mix of worker–task specialization and (2) linking people and tasks by the speed of the production line—resulted in huge savings in cost and huge increases in output that occur in large, organized work settings. For example, in 1908, managers at the Franklin Motor Company using scientific management principles redesigned the work process, and the output of cars increased from 100 cars a month to 45 cars a day; workers' wages, however, increased by only 90 percent.⁴

Taylor's work has had an enduring effect on the management of production systems. Managers in every organization, whether it produces goods or services, now carefully analyze the basic tasks that workers must perform and try to create a work environment that will allow their organizations to operate most efficiently. We discuss this important issue in Chapters 6 and 7.

Weber's Bureaucratic Theory

Side by side with scientific managers studying the person–task mix to increase efficiency, other researchers were focusing on how to increase the efficiency with which organizations were managed. Max Weber, a German professor of sociology, outlined his famous principles of **bureaucracy**—a formal system of organization and administration designed to ensure efficiency and effectiveness—and created bureaucratic theory. A bureaucratic system of administration is based on five principles:

- Principle 1: *In a bureaucracy, a manager's formal authority derives from the position he or she holds in the organization.*

Authority is the power to hold people accountable for their actions and to make decisions concerning the use of organizational resources. Authority gives managers the right to direct and control their subordinates' behavior to achieve organizational goals. In a bureaucratic system of administration, obedience is owed to a manager, not because of any personal qualities—such as personality, wealth, or social status—but because the manager occupies a position that is associated with a certain level of authority and responsibility.⁵

- Principle 2: *In a bureaucracy, people should occupy positions because of their performance, not because of their social standing or personal contacts.*

This principle was not always followed in Weber's time and is often ignored today. Some organizations and industries are still affected by social networks in which personal contacts and relations, not job-related skills, influence hiring and promotion decisions.

- Principle 3: *The extent of each position's formal authority and task responsibilities, and its relationship to other positions in an organization, should be clearly specified.*

When the tasks and authority associated with various positions in the organization are clearly specified, managers and workers know what is expected of them and what to expect from each other. Moreover, an organization can hold all its employees strictly accountable for their actions when they know their exact responsibilities.

- Principle 4: *Authority can be exercised effectively in an organization when positions are arranged hierarchically, so employees know whom to report to and who reports to them.⁶*

Managers must create an organizational hierarchy of authority that makes it clear who reports to whom and to whom managers and workers should go if conflicts or problems arise. This principle is especially important in the armed forces, FBI, CIA, and other organizations that deal with sensitive issues involving possible major repercussions. It is vital that managers at high levels of the hierarchy be able to hold subordinates accountable for their actions.

- Principle 5: *Managers must create a well-defined system of rules, standard operating procedures, and norms so that they can effectively control behavior within an organization.*

Rules are formal written instructions that specify actions to be taken under different circumstances to achieve specific goals (for example, if A happens, do B). **Standard operating procedures (SOPs)** are specific sets of written instructions about how to perform a certain aspect of a task. A rule might state that at the end of the workday employees are to leave their machines in good order, and a set of SOPs specifies exactly how they should do so, itemizing which machine parts must be oiled or replaced. **Norms** are unwritten, informal codes of conduct that prescribe how people should act in particular situations. For example, an organizational norm in a restaurant might be that waiters should help each other if time permits.

Rules, SOPs, and norms provide behavioral guidelines that increase the performance of a bureaucratic system because they specify the best ways to accomplish organizational tasks. Companies such as McDonald's and Wal-Mart have developed extensive rules and procedures to specify the behaviors required of their employees, such as "Always greet the customer with a smile."

Weber believed that organizations that implement all five principles establish a bureaucratic system that improves organizational performance. The specification of positions and the use of rules and SOPs to regulate how tasks are performed make it easier for managers to organize and control the work of subordinates. Similarly,

fair and equitable selection and promotion systems improve managers' feelings of security, reduce stress, and encourage organizational members to act ethically and further promote the interests of the organization.⁷

If bureaucracies are not managed well, many problems can result. Sometimes, managers allow rules and SOPs, "bureaucratic red tape," to become so cumbersome that decision making becomes slow and inefficient and organizations are unable to change. When managers rely too much on rules to solve problems and not enough on their own skills and judgment, their behavior becomes inflexible. A key challenge for managers is to use bureaucratic principles to benefit, rather than harm, an organization.

The Work of Mary Parker Follett

If F. W. Taylor is considered the father of management thought, Mary Parker Follett (1868–1933) serves as its mother.⁸ Much of her writing about management and the way managers should behave toward workers was a response to her concern that Taylor was ignoring the human side of the organization. She pointed out that management often overlooks the multitude of ways in which employees can contribute to the organization when managers allow them to participate and exercise initiative in their everyday work lives.⁹ Taylor, for example, never proposed that managers involve workers in analyzing their jobs to identify better ways to perform tasks, or even ask workers how they felt about their jobs. Instead, he used time and motion experts to analyze workers' jobs for them. Follett, in contrast, argued that because workers know the most about their jobs, they should be involved in job analysis and managers should allow them to participate in the work development process.



Mary Parker Follett, an early management thinker who advocated that "Authority should go with knowledge . . . whether it is up the line or down."

Follett proposed, "Authority should go with knowledge . . . whether it is up the line or down." In other words, if workers have the relevant knowledge, then workers, rather than managers, should be in control of the work process itself, and managers should behave as coaches and facilitators—not as monitors and supervisors. In making this statement, Follett anticipated the current interest in self-managed teams and empowerment. She also recognized the importance of having managers in different departments communicate directly with each other to speed decision making. She advocated what she called "cross-functioning": members of different departments working together in cross-departmental teams to accomplish projects—an approach that is increasingly utilized today.¹⁰ She proposed that knowledge and expertise, not managers' formal authority deriving from their position in the hierarchy, should decide who would lead at any particular moment. She believed, as do many management theorists today, that power is fluid and should flow to the person who can best help the organization achieve its goals. Follett took a horizontal view of power and authority, rather than viewing the vertical chain of command as being most essential to effective management. Thus, Follett's approach was very radical for its time.

The Hawthorne Studies and Human Relations

Probably because of its radical nature, Follett's work went unappreciated by managers and researchers until quite recently. Most continued to follow in the footsteps of Taylor, and to increase efficiency, they studied ways to improve various characteristics of the work setting, such as job specialization or the kinds of tools workers used. One series of studies was conducted from 1924 to 1932 at the Hawthorne Works of the Western Electric Company.¹¹

This research, now known as the Hawthorne studies, was initiated as an attempt to investigate how characteristics of the work setting—specifically the level of lighting or illumination—affect worker fatigue and performance. The researchers conducted an experiment in which they systematically measured worker productivity at various levels of illumination.

The experiment produced some unexpected results. The researchers found that regardless of whether they raised or lowered the level of illumination, productivity increased. In fact, productivity began to fall only when the level of illumination dropped to the level of moonlight, a level at which presumably workers could no longer see well enough to do their work efficiently.

As you can imagine, the researchers found these results very puzzling. They invited a noted Harvard psychologist, Elton Mayo, to help them. Mayo proposed another series of experiments to solve the mystery. These experiments, known as the relay assembly test experiments, were designed to investigate the effects of other aspects of the work context on job performance, such as the effect of the number and length of rest periods and hours of work on fatigue and monotony.¹² The goal was to raise productivity.

During a two-year study of a small group of female workers, the researchers again observed that productivity increased over time, but the increases could not be solely attributed to the effects of changes in the work setting. Gradually, the researchers discovered that, to some degree, the results they were obtaining were influenced by the fact that the researchers themselves had become part of the experiment. In other words, the presence of the researchers was affecting the results because the workers enjoyed receiving attention and being the subject of study and were willing to cooperate with the researchers to produce the results they believed the researchers desired.

Subsequently, it was found that many other factors also influence worker behavior, and it was not clear what was actually influencing Hawthorne workers' behavior. However, this particular effect—which became known as the **Hawthorne effect**—seemed to suggest that the attitudes of workers toward their managers affect the level of workers' performance. In particular, the significant finding was that a manager's behavior or leadership approach can affect performance. This finding led many researchers to turn their attention to managerial behavior and leadership. If supervisors could be trained to behave in ways that would elicit cooperative behavior from their subordinates, then productivity could be increased. From this view emerged the **human relations movement**, which advocates that supervisors be behaviorally trained to manage subordinates in ways that elicit their cooperation and increase their productivity.

The importance of behavioral or human relations training became even clearer to its supporters after another series of experiments—the bank wiring room experiments. In a study of workers making telephone-switching equipment, researchers Elton Mayo and F. J. Roethlisberger discovered that the workers, as a group, had

deliberately adopted a norm of output restriction to protect their jobs. Other group members subjected workers who violated this informal production norm to sanctions. Those who violated group performance norms and performed above the norm were called “ratebusters”; those who performed below the norm were called “chisellers.”

The experimenters concluded that both types of workers threatened the group as a whole. Ratebusters threaten group members because they reveal to managers how fast the work can be done. Chisellers are looked down on because they are not doing their share of the work. Work-group members discipline both ratebusters and chisellers in order to create a pace of work that the workers (not the managers) think is fair. Thus, the work group’s influence over output can be as great as the supervisors’ influence. Since the work group can influence the behavior of its members, some management theorists argue that supervisors should be trained to behave in ways that gain the goodwill and cooperation of workers so that supervisors, not workers, control the level of work-group performance.

One of the main implications of the Hawthorne studies was that the behavior of managers and workers in the work setting is as important in explaining the level of performance as the technical aspects of the task. Managers must understand the workings of the **informal organization**, the system of behavioral rules and norms that emerge in a group, when they try to manage or change behavior in organizations. Many studies have found that, as time passes, groups often develop elaborate procedures and norms that bond members together, allowing unified action either to cooperate with management in order to raise performance or to restrict output and thwart the attainment of organizational goals.¹³ The Hawthorne studies demonstrated the importance of understanding how the feelings, thoughts, and behavior of work-group members and managers affect performance. It was becoming increasingly clear to researchers that understanding behavior in organizations is a complex process that is critical to increasing performance.¹⁴ Indeed, the increasing interest in the area of management known as **organizational behavior**, the study of the factors that have an impact on how individuals and groups respond to and act in organizations, dates from these early studies.

Theory X and Theory Y

Several studies after the Second World War revealed how assumptions about workers’ attitudes and behavior affect managers’ behavior. Douglas McGregor developed the most influential approach. He proposed that two different sets of assumptions about work attitudes and behaviors dominate the way managers think and affect how they behave in organizations. McGregor named these two contrasting sets of assumptions *Theory X* and *Theory Y*.¹⁵

According to the assumptions of **Theory X**, the average worker is lazy, dislikes work, and will try to do as little as possible. Moreover, workers have little ambition and wish to avoid responsibility. Thus, the manager’s task is to counteract workers’ natural tendencies to avoid work. To keep workers’ performance at a high level, the manager must supervise them closely and control their behavior by means of “the carrot and stick”—rewards and punishments.

Managers who accept the assumptions of Theory X design and shape the work setting to maximize their control over workers’ behaviors and minimize workers’ control over the pace of work. These managers believe that workers must be made to do what is necessary for the success of the organization, and they focus on

developing rules, SOPs, and a well-defined system of rewards and punishments to control behavior. They see little point in giving workers autonomy to solve their own problems because they think that the workforce neither expects nor desires cooperation. Theory X managers see their role as to closely monitor workers to ensure that they contribute to the production process and do not threaten product quality. Henry Ford, who closely supervised and managed his workforce, fits McGregor's description of a manager who holds Theory X assumptions.

In contrast, **Theory Y** assumes that workers are not inherently lazy, do not naturally dislike work, and, if given the opportunity, will do what is good for the organization. According to Theory Y, the characteristics of the work setting determine whether workers consider work to be a source of satisfaction or punishment; and managers do not need to closely control workers' behavior in order to make them perform at a high level, because workers will exercise self-control when they are committed to organizational goals. The implication of Theory Y, according to McGregor, is that "the limits of collaboration in the organizational setting are not limits of human nature but of management's ingenuity in discovering how to realize the potential represented by its human resources."¹⁶ It is the manager's task to create a work setting that encourages commitment to organizational goals and provides opportunities for workers to be imaginative and to exercise initiative and self-direction.

When managers design the organizational setting to reflect the assumptions about attitudes and behavior suggested by Theory Y, the characteristics of the organization are quite different from those of an organizational setting based on Theory X. Managers who believe that workers are motivated to help the organization reach its goals can decentralize authority and give more control over the job to workers, both as individuals and in groups. In this setting, individuals and groups are still accountable for their activities, but the manager's role is not to control employees but to provide support and advice, to make sure workers have the resources they need to perform their jobs, and to evaluate them on their ability to help the organization meet its goals. The same kinds of debates are raging today as managers seek to increase both the efficiency and effectiveness of their organizations.

CHAPTER

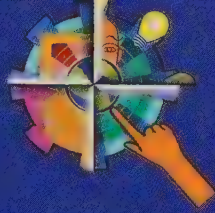
2

Values, Attitudes, Emotions, and Culture: The Manager as a Person

Learning Objectives

After studying this chapter, you should be able to:

- Describe the various personality traits that affect how managers think, feel, and behave.
- Explain what values and attitudes are and describe their impact on managerial action.
- Appreciate how moods and emotions influence all members of an organization.
- Describe the nature of emotional intelligence and its role in management.
- Define organizational culture and explain how managers both create and are influenced by organizational culture.



Management Snapshot

Employees Come First at PAETEC

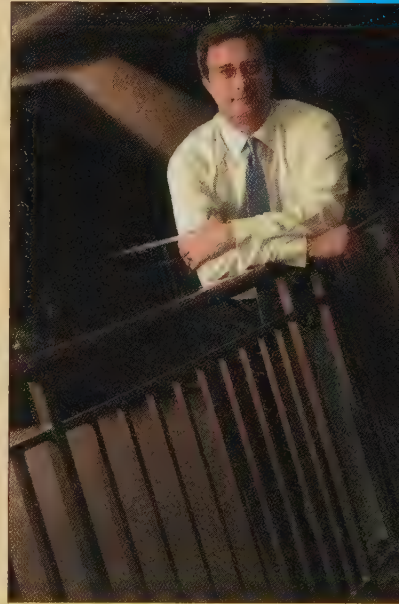
How can managers in troubled industries promote organizational growth and effectiveness?

PAETEC Communications is a privately-owned broadband telecommunications company that provides local, long distance, data, and Internet services in 27 markets across the United States.¹ When PAETEC was founded in 1998, it had less than 20 employees and revenues of only \$150,000; by 2004, it had 1,000 employees and \$360 million in revenues.² Moreover, this phenomenal rate of growth occurred during a period when the telecommunications industry lost over 500,000 jobs.³

PAETEC's growth and ongoing success are a tribute to the values of its five founders and the culture they created. In particular, Arunas Chesonis, one of the founders and its current CEO, ensures that PAETEC's values are upheld by using them to guide the way he manages on a day-to-day basis. The result is a satisfied, motivated, and loyal workforce whose members have developed a unique and distinct approach to the way they perform their jobs.⁴

An overarching principle at PAETEC is "Employees come first."⁵ This does not mean that PAETEC doesn't care about customers; nothing could be further from the truth. Chesonis believes that when a company takes good care of its employees, they will take good care of their customers. For Chesonis, putting employees first means helping them attain a well-balanced and prosperous work and family life, providing them with deserved

recognition and admiration, and fostering open communication and helping behavior.⁶ Chesonis also believes that all employees should be treated with respect and as equals. Managers at PAETEC do not receive special perks, and pay differentials between managers and non-managers are deliberately kept relatively low.



PAETEC founder and current CEO Arunas Chesonis believes that when a company takes good care of its employees, they will take good care of their customers.

Chesonis takes daily walks around PAETEC's headquarters in Rochester, New York, talking with employees, answering questions, and recognizing accomplishments. Accomplishments are also recognized through two kinds of special awards, Maestro Awards and Chairman Awards. Maestro Awards of stock options are given to recognize outstanding employee accomplishments. Employees who have sustained levels of exceptional performance receive the Chairman Award, a \$5,000 award that might include a Rolex watch or a luxury vacation. The contributions of all employees are recognized with an annual 10 percent bonus;⁷ PAETEC pays out around \$3.5 million in bonuses each year.⁸

Chesonis also nurtures a culture of cooperation and open communication in which every employee voluntarily offers help when it is

needed. Employees are expected to share their knowledge, and Chesonis strives to eliminate boundaries between departments and units. True to this culture, Chesonis has a companywide conference call every two weeks in which he shares up-to-date information with employees and solicits and answers their questions. More often than not, the information he conveys is the kind that managers in other companies rarely, if ever, would share with their employees.⁹

Chesonis's values and PAETEC's culture emphasize putting employees first; this employee-centered approach makes good business sense. Employees at PAETEC really want the company to continue to grow and succeed; they are highly motivated and committed to providing the best service they can to their customers.¹⁰

Overview

Like people everywhere, Arunas Chesonis has his own distinctive personality, values, ways of viewing things, and personal challenges and disappointments. In this chapter, we focus on the manager as a feeling, thinking human being. We start by describing enduring characteristics that influence how managers "manage," as well as how they view other people, their organizations, and the world around them. We discuss as well how managers' values, attitudes, and moods play out in organizations, shaping organizational culture. By the end of this chapter, you will have a good appreciation of how the personal characteristics of managers influence the process of management in general and organizational culture in particular.

Enduring Characteristics: Personality Traits

personality traits

Enduring tendencies to feel, think, and act in certain ways.

All people, including managers, have certain enduring characteristics that influence how they think, feel, and behave both on and off the job. These characteristics are **personality traits**, particular tendencies to feel, think, and act in certain ways that can be used to describe the personality of every individual. It is important to understand the personalities of managers because their personalities influence their behavior and their approach to managing people and resources.

Some managers, like Procter & Gamble's former chairman Edwin Artzt, are demanding, difficult to get along with, and highly critical of other people.¹¹ Other managers, like Southwest Airlines' former CEO Herb Kelleher, may be as concerned about effectiveness and efficiency as highly critical managers but are easier to get along with, are likable, and frequently praise the people around them. Both styles of management may produce excellent results, but their effects on employees are quite different. Do managers deliberately decide to adopt one or the other of these approaches to management? Although they may do so part of the time, in all

likelihood their personalities also account for their different approaches. Indeed, research suggests that the way people react to different conditions depends, in part, on their personalities.¹²

The Big Five personality traits

We can think of an individual's personality as being composed of five general traits or characteristics: extraversion, negative affectivity, agreeableness, conscientiousness, and openness to experience.¹³ Researchers often consider these the Big Five personality traits.¹⁴ Each of them can be viewed as a continuum along which every individual or, more specifically, every manager falls (see Figure 2.1).

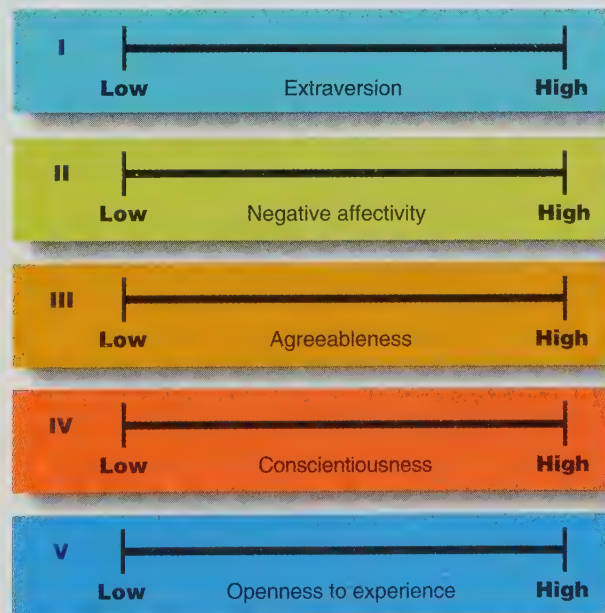
Some managers may be at the high end of one trait continuum, others at the low end, and still others somewhere in between. An easy way to understand how these traits can affect a person's approach to management is to describe what people are like at the high and low ends of each trait continuum. As will become evident as you read about each trait, no single trait is right or wrong for being an effective manager. Rather, effectiveness is determined by a complex interaction between the characteristics of managers (including personality traits) and the nature of the job and organization in which they are working. Moreover, personality traits that enhance managerial effectiveness in one situation may actually impair it in another situation.

extraversion The tendency to experience positive emotions and moods and to feel good about oneself and the rest of the world.

EXTRAVERSION **Extraversion** is the tendency to experience positive emotions and moods and feel good about oneself and the rest of the world. Managers who are high on extraversion (often called *extraverts*) tend to be sociable,

Figure 2.1
The Big Five Personality Traits

Manager's personalities can be described by determining which point on each of the following dimensions best characterizes the manager in question:



negative

affectivity The tendency to experience negative emotions and moods, to feel distressed, and to be critical of oneself and others.

affectionate, outgoing, and friendly. Managers who are low on extraversion (often called *introverts*) tend to be less inclined toward social interactions and to have a less positive outlook. Being high on extraversion may be an asset for managers whose jobs entail especially high levels of social interaction. Managers who are low on extraversion may nevertheless be highly effective and efficient, especially when their jobs do not require excessive social interaction. Their more “quiet” approach may enable them to accomplish quite a bit of work in limited time. See Figure 2.2 for an example of a scale that can be used to measure a person’s level of extraversion.

NEGATIVE AFFECTIVITY **Negative affectivity** is the tendency to experience negative emotions and moods, feel distressed, and be critical of oneself and

Figure 2.2
Measures of
Extraversion,
Agreeableness
and Conscientiousness

Listed below are phrases describing people’s behaviors. Please use the rating scale below to describe how accurately each statement describes *you*. Describe yourself as you generally are now, not as you wish to be in the future. Describe yourself as you honestly see yourself, in relation to other people you know of the same sex as you are and roughly your same age.

1	2	3	4	5
Very inaccurate	Moderately inaccurate	Neither inaccurate nor accurate	Moderately accurate	Very accurate

- | | |
|--|---|
| ___ 1. Am interested in people. | ___ 17. Often forget to put things back in their proper place.* |
| ___ 2. Am always prepared. | ___ 18. Have little to say.* |
| ___ 3. Am not really interested in others.* | ___ 19. Take time out for others. |
| ___ 4. Leave my belongings around.* | ___ 20. Like order. |
| ___ 5. Am the life of the party. | ___ 21. Talk to a lot of different people at parties. |
| ___ 6. Sympathize with others’ feelings. | ___ 22. Feel little concern for others.* |
| ___ 7. Don’t talk a lot.* | ___ 23. Shirk my duties.* |
| ___ 8. Pay attention to details. | ___ 24. Don’t like to draw attention to myself.* |
| ___ 9. Insult people.* | ___ 25. Feel others’ emotions. |
| ___ 10. Make a mess of things.* | ___ 26. Follow a schedule. |
| ___ 11. Feel comfortable around people. | ___ 27. Don’t mind being the center of attention. |
| ___ 12. Have a soft heart. | ___ 28. Make people feel at ease. |
| ___ 13. Get chores done right away. | ___ 29. Am exacting in my work. |
| ___ 14. Keep in the background.* | ___ 30. Am quiet around strangers.* |
| ___ 15. Start conversations. | |
| ___ 16. Am not interested in other people’s problems.* | |

* Item is reverse-scored: 1 = 5, 2 = 4, 4 = 2, 5 = 1

Scoring: Sum responses to items for an overall scale.

Extraversion = sum of items 5, 7, 11, 14, 15, 18, 21, 24, 27, 30

Agreeableness = sum of items 1, 3, 6, 9, 12, 16, 19, 22, 25, 28

Conscientiousness = sum of items 2, 4, 8, 10, 13, 17, 20, 23, 26, 29

others. Managers high on this trait may often feel angry and dissatisfied and complain about their own and others' lack of progress. Managers who are low on negative affectivity do not tend to experience many negative emotions and moods and are less pessimistic and critical of themselves and others. On the plus side, the critical approach of a manager high on negative affectivity may sometimes be effective if it spurs both the manager and others to improve their performance. Nevertheless, it is probably more pleasant to work with a manager who is low on negative affectivity; the better working relationships that such a manager is likely to cultivate also can be an important asset. Figure 2.3 is an example of a scale developed to measure a person's level of negative affectivity.

agreeableness The tendency to get along well with other people.

AGREEABLENESS **Agreeableness** is the tendency to get along well with others. Managers who are high on the agreeableness continuum are likable, tend to be affectionate, and care about other people. Managers who are low on agreeableness

Figure 2.3
A Measure of
Negative
Affectivity

Instructions: Listed below are a series of statements a person might use to describe her/his attitudes, opinions, interests, and other characteristics. If a statement is true or largely true, put a "T" in the space next to the item. Or if the statement is false or largely false, mark an "F" in the space.

Please answer every statement, even if you are not completely sure of the answer. Read each statement carefully, but don't spend too much time deciding on the answer.

- | | |
|---|---|
| _____ 1. I often find myself worrying about something. | _____ 9. I sometimes get myself into a state of tension and turmoil as I think of the day's events. |
| _____ 2. My feelings are hurt rather easily. | |
| _____ 3. Often I get irritated at little annoyances. | _____ 10. Minor setbacks sometimes irritate me too much. |
| _____ 4. I suffer from nervousness. | _____ 11. I often lose sleep over my worries. |
| _____ 5. My mood often goes up and down. | _____ 12. There are days when I'm "on edge" all of the time. |
| _____ 6. I sometimes feel "just miserable" for no good reason. | _____ 13. I am too sensitive for my own good. |
| _____ 7. Often I experience strong emotions—anxiety, anger—without really knowing what causes them. | _____ 14. I sometimes change from happy to sad, or vice versa, without good reason. |
| _____ 8. I am easily startled by things that happen unexpectedly. | |

Scoring: Level of negative affectivity is equal to the number of items answered "True."

may be somewhat distrustful of others, unsympathetic, uncooperative, and even at times antagonistic. Being high on agreeableness may be especially important for managers whose responsibilities require that they develop good, close relationships with others. Nevertheless, a low level of agreeableness may be an asset in managerial jobs that actually require that managers be antagonistic, such as drill sergeants, and some other kinds of military managers. See Figure 2.2 for an example of a scale that measures a person's level of agreeableness.

conscientiousness

The tendency to be careful, scrupulous, and persevering.

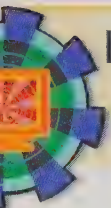
CONSCIENTIOUSNESS **Conscientiousness** is the tendency to be careful, scrupulous, and persevering.¹⁵ Managers who are high on the conscientiousness continuum are organized and self-disciplined; those who are low on this trait might sometimes appear to lack direction and self-discipline. Conscientiousness has been found to be a good predictor of performance in many kinds of jobs, including managerial jobs in a variety of organizations.¹⁶ CEOs of major companies, such as Carly Fiorino of Hewlett-Packard and Samuel J. Palmisano of IBM, often show signs of being high on conscientiousness—the long hours they work, their attention to detail, and their ability to handle their multiple responsibilities in an organized manner. Figure 2.2 provides an example of a scale that measures conscientiousness.

openness to experience

The tendency to be original, have broad interests, be open to a wide range of stimuli, be daring, and take risks.

OPENNESS TO EXPERIENCE **Openness to experience** is the tendency to be original, have broad interests, be open to a wide range of stimuli, be daring, and take risks.¹⁷ Managers who are high on this trait continuum may be especially likely to take risks and be innovative in their planning and decision making. Entrepreneurs who start their own businesses—like Bill Gates of Microsoft, Jeff Bezos of Amazon.com, and Anita Roddick of The Body Shop—are, in all likelihood, high on openness to experience, which has contributed to their success as entrepreneurs and managers. Arunas Chesonis, discussed in this chapter's "Management Snapshot," founded his own company and continues to explore new ways for it to grow—a testament to his high level of openness to experience. Managers who are low on openness to experience may be less prone to take risks and more conservative in their planning and decision making. In certain organizations and positions, this tendency might be an asset. The manager of the fiscal office in a public university, for example, must ensure that all university departments and units follow the university's rules and regulations pertaining to budgets, spending accounts, and reimbursements of expenses.

Managers who initiate major changes in their organizations often are high on openness to experience, as is true of IBM CEO and chairman Samuel Palmisano, profiled in the following "Information Technology Byte."



Information Technology Byte

Sam Palmisano Reinvents IBM

Samuel Palmisano started his career at IBM over 30 years ago as a sales representative. He went on to head many of IBM's major divisions before becoming CEO in 2002 and chairman of the board in 2004.¹⁸ Palmisano is spearheading a major redirection of IBM that changes the company's focus and activities in fundamental ways. Essentially, he is transforming IBM from being a hardware and software provider to being a business solution provider to corporate customers.¹⁹ Thus, IBM is focusing on developing close, long-term relationships with customers that will enable it to help them with their pressing business problems,

problems ranging from purchasing and marketing to production and customer service. In becoming close to its customers and helping them meet their business needs, IBM will also be providing them with its mainstay hardware and software. But the latter is part of a bigger package oriented around being a total-solution provider to meet customers' business needs.²⁰

To accomplish this aim, Palmisano has taken many bold steps. For example, IBM acquired Pricewaterhouse Coopers and Rational Software in 2002 at a cost of over \$5.5 billion. These acquisitions will help IBM provide more high-level, all-encompassing consulting-type services to its customers. Realizing that these changes will require changes in the mindsets and skills of employees, Palmisano spent \$800 million on employee education in 2004.²¹

Palmisano is encouraging IBM managers to go out and talk to customers, learn about their business needs, and develop comprehensive solutions to meet them. The solutions should be the kind that address a fundamental problem organizations in a particular industry face and, thus, can be sold to other companies in that industry. As Palmisano puts it, "If they got out there and actually solved the problem with the client . . . they would understand what they needed to do." For example, while IBM has sold hardware and data center services to FinnAir for years, now it has begun using mathematical modeling to help FinnAir improve customer loyalty while reducing marketing costs—a major pressing concern for FinnAir today.²²



Sam Palmisano spent over 30 years as a sales representative for IBM. Now, as CEO, he is encouraging IBM managers go out and talk to customers to learn about their needs.

Interestingly enough, Palmisano's personality and management style are very different from those of his highly successful predecessor, former CEO Lou Gerstner. While Gerstner was formal and direct, Palmisano is more relaxed and understated. Industry watchers suggest that Palmisano's bold changes are right on track with where the hardware and software industry needs to be headed, and competitors like Hewlett-Packard and Microsoft seem to be copying some of his initiatives. While time will tell if Palmisano's vision for the new IBM will deliver on its promises, his openness to experience contributes to his confidence that "we are on the verge of the next great opportunity for our company, and for the entire information technology industry."²³

By now it should be clear that successful managers like Palmisano and Gerstner occupy a variety of positions on the Big Five personality-trait continua. One highly effective manager may be high on extraversion and negative affectivity, another equally effective manager may be low on both these traits, and still another may be somewhere in between. Members of an organization must understand these differences among managers because they can shed light on how managers behave and on their approach to planning, leading, organizing, or controlling. If subordinates realize, for example, that their manager is low on extraversion, they will not feel slighted when their manager seems to be aloof because they will realize that by nature he or she is simply not outgoing.

Managers themselves also need to be aware of their own personality traits and the traits of others, including their subordinates and fellow managers. A manager who knows that he has a tendency to be highly critical of other people might try to tone down his negative approach. Similarly, a manager who realizes that her chronically complaining subordinate tends to be so negative because of his personality may take all his complaints with a grain of salt and realize that things probably are not as bad as this subordinate says they are.

In order for all members of an organization to work well together and with people outside the organization, such as customers and suppliers, they must understand each other. Such understanding comes, in part, from an appreciation of some of the fundamental ways in which people differ from one another—that is, an appreciation of personality traits.

Other personality traits that affect managerial behavior

Many other specific traits in addition to the Big Five describe people's personalities. Here we look at traits that are particularly important for understanding managerial effectiveness: locus of control; self-esteem; and the needs for achievement, affiliation, and power.

internal locus of control The tendency to locate responsibility for one's fate within oneself.

LOCUS OF CONTROL People differ in their views about how much control they have over what happens to and around them. The locus-of-control trait captures these beliefs.²⁴ People with an **internal locus of control** believe that they themselves are responsible for their own fate; they see their own actions and behaviors as being major and decisive determinants of important outcomes such as attaining levels of job performance, being promoted, or being turned down for a choice job assignment. Some managers with an internal locus of control see the success of a whole organization resting on their shoulders. One example is Arunas Chesonis in the “Management Snapshot.” An internal locus of control also helps to ensure ethical behavior and decision making in an organization because people feel accountable and responsible for their own actions. Managers with an internal locus may also feel obligated to expose wrongdoing in an organization, even if they are personally not responsible for it, as indicated in the following “Ethics in Action.”



Ethics in Action

Taking Responsibility for Exposing Wrongdoing

Noreen Harrington, a former fund manager at the Hartz Group investment firm based in Secaucus, New Jersey, became aware of illegal activity in the firm by overhearing traders discussing after-hours trades. These traders managed hedge funds—investment funds that hold a variety of types of financial assets to offset risks and provide a consistent return to shareholders.²⁵ Harrington was not involved in these hedge funds herself but could not help overhearing the traders. From their conversation, she learned that some mutual fund managers were allowing the traders to buy and sell their shares in the fund after the market had closed.²⁶ This is illegal and unethical and gave the traders an unfair advantage over other investors in the mutual funds, who were able to trade only when the market was open.

Harrington told Edward J. Stern, a member of the Stern family that owns the Hartz Group, what she had overheard but this changed nothing—the illegal trading carried on. Harrington resigned but kept an eye on the news, hoping that security regulators would uncover what she had witnessed.²⁷

After a year of waiting, Harrington felt a responsibility to report the illegal trading, as it was most likely still going on and hurting ordinary investors. She relayed what she had observed as a Hartz manager to Eliot Spitzer, the New York State attorney general. Spitzer's investigation of her claim led the Stern family to settle the case for \$40 million, although they admitted no wrongdoing. In taking responsibility for exposing what she knew was wrong, Harrington set events in motion that ultimately had a major impact on the mutual fund industry as a whole: Other funds were scrutinized and additional instances of after-hours trading were uncovered.²⁸ As Spitzer puts it, "Because of her gutsy move, there will be dramatic reform in a sector that has the life savings of 95 million Americans."²⁹

external locus of control

The tendency to locate responsibility for one's fate in outside forces and to believe that one's own behavior has little impact on outcomes.

self-esteem The degree to which individuals feel good about themselves and their capabilities.

need for achievement The extent to which an individual has a strong desire to perform challenging tasks well and to meet personal standards for excellence.

need for affiliation The extent to which an individual is concerned about establishing and maintaining good interpersonal relations, being liked, and having other people get along.

need for power The extent to which an individual desires to control or influence others.

People with an **external locus of control** believe that outside forces are responsible for what happens to and around them; they do not think that their own actions make much of a difference. As such, they tend not to intervene to try to change a situation or solve a problem, leaving it to someone else.

Managers need to have an internal locus of control because they are responsible for what happens in organizations; they need to believe that they can and do make a difference, as does Arunas Chesonis at PAETEC Communications. Moreover, managers are responsible for ensuring that organizations and their members behave in an ethical fashion, and for this as well they need to have an internal locus of control—they need to know and feel they can make a difference.

SELF-ESTEEM **Self-esteem** is the degree to which individuals feel good about themselves and their capabilities. People with high self-esteem believe that they are competent, deserving, and capable of handling most situations, as does Arunas Chesonis. People with low self-esteem have poor opinions of themselves, are unsure about their capabilities, and question their ability to succeed at different endeavors.³⁰ Research suggests that people tend to choose activities and goals consistent with their levels of self-esteem. High self-esteem is desirable for managers because it facilitates their setting and keeping high standards for themselves, pushes them ahead on difficult projects, and gives them the confidence they need to make and carry out important decisions.

NEEDS FOR ACHIEVEMENT, AFFILIATION, AND POWER Psychologist David McClelland has extensively researched the needs for achievement, affiliation, and power.³¹ The **need for achievement** is the extent to which an individual has a strong desire to perform challenging tasks well and to meet personal standards for excellence. People with a high need for achievement often set clear goals for themselves and like to receive performance feedback. The **need for affiliation** is the extent to which an individual is concerned about establishing and maintaining good interpersonal relations, being liked, and having the people around him or her get along with one another. The **need for power** is the extent to which an individual desires to control or influence others.³²

Research suggests that high needs for achievement and for power are assets for first-line and middle managers, and that a high need for power is especially important for upper-level managers.³³ One study found that U.S. presidents with a relatively high need

for power tended to be especially effective during their terms of office.³⁴ A high need for affiliation may not always be desirable in managers because it might lead them to try too hard to be liked by others (including subordinates) rather than doing all they can to ensure that performance is as high as it can and should be. Although most research on these needs has been done in the United States, some studies suggest that these findings may also be applicable to people in other countries such as India and New Zealand.³⁵

Taken together, these desirable personality traits for managers—an internal locus of control, high self-esteem, and high needs for achievement and power—suggest that managers need to be take-charge people who not only believe that their own actions are decisive in determining their own and their organizations' fates but also believe in their own capabilities. Such managers have a personal desire for accomplishment and influence over others.

Values, Attitudes, and Moods and Emotions

What are managers striving to achieve? How do they think they should behave? What do they think about their jobs and organizations? And how do they actually feel at work? Some answers to these questions can be found by exploring managers' values, attitudes, and moods.

Values, attitudes, and moods and emotions capture how managers experience their jobs as individuals. *Values* describe what managers are trying to achieve through work and how they think they should behave. *Attitudes* capture their thoughts and feelings about their specific jobs and organizations. *Moods and emotions* encompass how managers actually feel when they are managing. Although these three aspects of managers' work experience are highly personal, they also have important implications for understanding how managers behave, how they treat and respond to others, and how, through their efforts, they help contribute to organizational effectiveness through planning, leading, organizing, and controlling.

terminal value A lifelong goal or objective that an individual seeks to achieve.

instrumental value A mode of conduct that an individual seeks to follow.

norms Informal rules of conduct for behaviors considered important by most members of a group or organization.

value system The terminal and instrumental values that are guiding principles in an individual's life.

Values: terminal and instrumental

The two kinds of personal values are *terminal* and *instrumental*. A **terminal value** is a personal conviction about lifelong goals or objectives; an **instrumental value** is a personal conviction about desired modes of conduct or ways of behaving.³⁶ Terminal values often lead to the formation of **norms**, or informal rules of conduct, for behaviors considered important by most members of a group or organization, such as behaving honestly or courteously.

Milton Rokeach, one of the leading researchers in the area of human values, identified 18 terminal values and 18 instrumental values that describe each person's value system (see Figure 2.4).³⁷ By rank ordering the terminal values from 1 (most important as a guiding principle in one's life) to 18 (least important as a guiding principle in one's life) and then rank ordering the instrumental values from 1 to 18, people can give good pictures of their **value systems**—what they are striving to achieve in life and how they want to behave.³⁸ (You can gain a good understanding of your own values by rank ordering first the terminal values and then the instrumental values listed in Figure 2.4.)

Several of the terminal values listed in Figure 2.4 seem to be especially important for managers—such as *a sense of accomplishment (a lasting contribution)*, *equality (brotherhood, equal opportunity for all)*, and *self-respect (self-esteem)*. A manager who

Figure 2.4
Terminal and Instrumental Values

Terminal Values	Instrumental Values
A comfortable life (a prosperous life) An exciting life (a stimulating, active life) A sense of accomplishment (lasting contribution) A world at peace (free of war and conflict) A world of beauty (beauty of nature and the arts) Equality (brotherhood, equal opportunity for all) Family security (taking care of loved ones) Freedom (independence, free choice) Happiness (contentedness) Inner harmony (freedom from inner conflict) Mature love (sexual and spiritual intimacy) National security (protection from attack) Pleasure (an enjoyable, leisurely life) Salvation (saved, eternal life) Self-respect (self-esteem) Social recognition (respect, admiration) True friendship (close companionship) Wisdom (a mature understanding of life)	Ambitious (hard-working, aspiring) Broad-minded (open-minded) Capable (competent, effective) Cheerful (lighthearted, joyful) Clean (neat, tidy) Courageous (standing up for your beliefs) Forgiving (willing to pardon others) Helpful (working for the welfare of others) Honest (sincere, truthful) Imaginative (daring, creative) Independent (self-reliant, self-sufficient) Intellectual (intelligent, reflective) Logical (consistent, rational) Loving (affectionate, tender) Obedient (dutiful, respectful) Polite (courteous, well-mannered) Responsible (dependable, reliable) Self-controlled (restrained, self-disciplined)

Source: Reprinted with permission of The Free Press, a Division of Simon & Schuster Adult Publishing Group, from *The Nature of Human Values* by Milton Rokeach. Copyright © 1973 by The Free Press. All rights reserved.

thinks a sense of accomplishment is of paramount importance might focus on making a lasting contribution to an organization by developing a new product that can save or prolong lives, as is true of managers at Medtronic (a company that makes medical devices such as cardiac pacemakers), or by opening a new foreign subsidiary. A manager who places equality at the top of his or her list of terminal values may be at the forefront of an organization's efforts to support, provide equal opportunities to, and capitalize on the many talents of an increasingly diverse workforce.

Other values are likely to be considered important by many managers, such as *a comfortable life (a prosperous life)*, *an exciting life (a stimulating, active life)*, *freedom (independence, free choice)*, and *social recognition (respect, admiration)*. The relative importance that managers place on each terminal value helps explain what they are striving to achieve in their organizations and what they will focus their efforts on.

Several of the instrumental values listed in Figure 2.3 seem to be important modes of conduct for managers, such as being *ambitious (hardworking, aspiring)*, *broad-minded (open-minded)*, *capable (competent, effective)*, *responsible (dependable, reliable)*, and *self-controlled (restrained, self-disciplined)*. Moreover, the relative importance a manager places on these and other instrumental values may be a significant determinant of actual behaviors on the job. A manager who considers being *imaginative (daring, creative)* to

be highly important, for example, is more likely to be innovative and take risks than is a manager who considers this to be less important (all else being equal). A manager who considers being *honest* (*sincere, truthful*) to be of paramount importance may be a driving force for taking steps to ensure that all members of a unit or organization behave ethically. As indicated in the following “Ethics in Action,” taking ethical action sometimes requires that managers be courageous in addition to being honest.



Ethics in Action

The Courage to Be Honest

Peter Scannell was a manager at a Boston-area call center of Putnam Investments when he observed something troubling: Putnam managers were allowing some retirement mutual fund investors to make illegal quick buy and sell trades to take advantage of short-term fluctuations in fund prices. In fact, some of these investors were regularly engaging in short-term trades even though this kind of trading was prohibited by Putnam’s own policies.³⁹

A few days after Scannell told his supervisor of his concerns, he was taken from his car and beaten up; the assailant was allegedly an investor engaged in the activity Scannell had reported to his supervisor. Scannell says that a manager at Putnam was dismayed by his concern over the trading abuses and seemed to threaten him. Even when Scannell approached regulators in the Boston office of the Securities and Exchange Commission (SEC), he felt that his efforts to uphold ethical standards were being resisted.⁴⁰

Scannell discussed his concerns about the SEC with his lawyer, and eventually Scannell met with the SEC. Scannell later testified to the Governmental Affairs subcommittee of the U.S. Senate about the reactions of Putnam managers to his allegations of unethical behavior and the initial unresponsiveness of the SEC.⁴¹

Scannell and others who have exposed instances of illegal activity and trading abuses regarding mutual funds recognize that these unethical actions end up hurting millions of honest people who invest in mutual funds. Senator Peter Fitzgerald of Illinois, head of the Senate subcommittee, suggests that mutual fund trading abuses represent “the world’s largest skimming operation . . . a trough from which fund managers, brokers and other insiders are steadily siphoning off an excessive slice of the nation’s household, college and retirement savings.”⁴² In Scannell’s case, his persistent efforts to halt the unethical trading at Putnam hinged not only on his honesty but also on his courage to stand up for what he believed to be right, no matter what the consequences would be for him personally.

All in all, managers’ value systems signify what managers as individuals are trying to accomplish and become in their personal lives and at work. Thus, managers’ value systems are fundamental guides to their behavior and efforts at planning, leading, organizing, and controlling.

Attitudes


attitude A collection of feelings and beliefs.

An **attitude** is a collection of feelings and beliefs. Like everyone else, managers have attitudes about their jobs and organizations, and these attitudes affect how they approach their jobs. Two of the most important attitudes in this context are job satisfaction and organizational commitment.

job satisfaction

The collection of feelings and beliefs that managers have about their current jobs.

JOB SATISFACTION **Job satisfaction** is the collection of feelings and beliefs that managers have about their current jobs.⁴³ Managers who have high levels of job satisfaction generally like their jobs, feel that they are being fairly treated, and believe that their jobs have many desirable features or characteristics (such as interesting work, good pay and job security, autonomy, or nice co-workers). Figure 2.5 (page 64) shows sample items from two scales that managers can use to measure job satisfaction. Levels of job satisfaction tend to increase as one moves up the hierarchy in an organization. Upper managers, in general, tend to be more satisfied with their jobs than entry-level employees. Managers' levels of job satisfaction can range from very low to very high and anywhere in between.



Focus on Diversity

Changing Attitudes

An interesting trend in job attitudes has been observed among some managers in their 20s and 30s. For example, after Sandi Garcia graduated from the University of Wyoming with a degree in marketing, she landed a good job in Florida and was soon promoted into the managerial ranks. By all counts, Garcia should have been satisfied with her job—she was advancing in the company, making good money, and doing the kind of work she had hoped to do. Ironically, Garcia found herself becoming increasingly dissatisfied with her job. Putting in 12-hour workdays was not unusual for Garcia, nor was it unusual for her to work during the weekends. Living a hectic, fast-paced life revolving around work soon made Garcia dream of a simpler life where she would have time to do things she enjoyed such as skiing, being with family and friends, and doing volunteer work. Garcia acted on her dream: She moved back to Wyoming, and is now more satisfied with a less demanding job at the Wyoming Business Council.⁴⁴

Gregg Steiner was a high-tech manager on the West Coast who seemed to have everything, including a Malibu beach house. However, he was dissatisfied with a job that left him no free time to enjoy the beach or much else. Steiner quit the high-tech world and works at his now more modest home, handling customer service for his family's diaper rash ointment business (Pinxav).⁴⁵

Young managers like Garcia and Steiner are not lazy, nor do they lack ambition. Rather, they have lived through changes in the corporate landscape that cause them to question what work should be and should mean to them. Some of these young managers have seen their parents slaving away at their jobs in corporate America year after year, only to be laid off in tough times. While their parents might never have questioned their commitment to their organizations, the need to work long hours, and the lack of time for much else other than work and raising a family, Garcia and Steiner desire the flexibility and time to live lives that are simpler but also richer in terms of meaningful activities. And they want to be in charge of their own lives rather than having their lives dictated by persons higher up the corporate hierarchy.⁴⁶

Of course, for every young manager like Garcia and Steiner who voluntarily leaves the fast track for a more balanced life, there are other young prospective managers eager to take their place in the corporate world. And a job that is dissatisfying for one manager might be satisfying for another. In any case, in an era when trust in corporations has come under question (e.g., due to ethical lapses and fraud at companies like Enron), some young managers are seeking to invest themselves in things they can really trust.⁴⁷

Figure 2.5
Sample Items
from Two
Measures of Job
Satisfaction

Sample items from the Minnesota Satisfaction Questionnaire:

People respond to each of the items in the scale by checking whether they are:

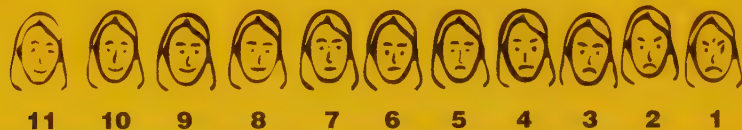
- | | |
|--|---|
| <input type="checkbox"/> Very dissatisfied | <input type="checkbox"/> Satisfied |
| <input type="checkbox"/> Dissatisfied | <input type="checkbox"/> Very satisfied |
| <input type="checkbox"/> Can't decide whether satisfied or not | |

On my present job, this is how I feel about . . .

- | | |
|---|---|
| ____ 1. Being able to do things that don't go against my conscience. | ____ 7. The chances for advancement on this job. |
| ____ 2. The way my job provides for steady employment. | ____ 8. The freedom to use my own judgment. |
| ____ 3. The chance to do things for other people. | ____ 9. The working conditions. |
| ____ 4. The chance to do something that makes use of my abilities. | ____ 10. The way my co-workers get along with each other. |
| ____ 5. The way company policies are put into practice. | ____ 11. The praise I get for doing a good job. |
| ____ 6. My pay and the amount of work I do. | ____ 12. The feeling of accomplishment I get from the job. |

The Faces Scale

Workers select the face which best expresses how they feel about their job in general.



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organizational citizenship behaviors (OCBs)

Behaviors that are not required of organizational members but that contribute to and are necessary for organizational efficiency, effectiveness, and gaining a competitive advantage.

In general, it is desirable for managers to be satisfied with their jobs, for at least two reasons. First, satisfied managers may be more likely to go the extra mile for their organization or perform **organizational citizenship behaviors (OCBs)**, behaviors that are not required of organizational members but that contribute to and are necessary for organizational efficiency, effectiveness, and gaining a competitive advantage.⁴⁸ Managers who are satisfied with their jobs are more likely to perform these “above and beyond the call of duty” behaviors, which can range from putting in extra-long hours when needed to coming up with truly creative ideas and overcoming obstacles to implement them (even when doing so is not part of the manager’s job) or to going out of his or her way to help a co-worker, subordinate, or superior (even when doing so entails considerable personal sacrifice).⁴⁹

A second reason why it is desirable for managers to be satisfied with their jobs is that satisfied managers may be less likely to quit.⁵⁰ A manager who is highly satisfied may never even think about looking for another position; a dissatisfied manager may always be on the lookout for new opportunities. Turnover can hurt an

organization because it results in the loss of the experience and knowledge that managers have gained about the company, industry, and business environment.

A growing source of dissatisfaction for many lower- and middle-level managers, as well as for nonmanagerial employees, is the threat of unemployment and increased workloads from organizational downsizings. A recent study of 4,300 workers conducted by Wyatt Co. found that 76 percent of the employees of expanding companies are satisfied with their jobs but only 57 percent of the employees of companies that have downsized are satisfied.⁵¹ Organizations that try to improve their efficiency through restructuring often eliminate a sizable number of first-line and middle management positions. This decision obviously hurts the managers who are laid off, and it also can reduce the job satisfaction levels of managers who remain. They might fear that they may be the next to be let go. In addition, the workloads of remaining managers often are dramatically increased as a result of restructuring, and this also can contribute to dissatisfaction.

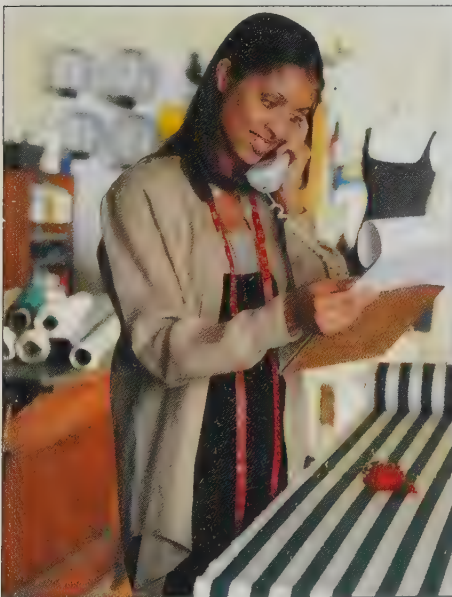
organizational commitment The collection of feelings and beliefs that managers have about their organization as a whole.

ORGANIZATIONAL COMMITMENT **Organizational commitment** is the collection of feelings and beliefs that managers have about their organization as a whole. Managers who are committed to their organizations believe in what their organizations are doing, are proud of what these organizations stand for, and feel a high degree of loyalty toward their organizations. Committed managers are more likely to go above and beyond the call of duty to help their company and are less likely to quit.⁵² Organizational commitment can be especially strong when employees and managers truly believe in organizational values; it also leads to a strong organizational culture, as found in PAETEC.

Organizational commitment is likely to help managers perform some of their figurehead and spokesperson roles (see Chapter 1). It is much easier for a manager to persuade others both inside and outside the organization of the merits of what the organization has done and is seeking to accomplish if the manager truly believes in and is committed to the organization. Figure 2.6 is an example of a scale that managers can use to measure a person's level of organizational commitment.

Do managers in different countries have similar or different attitudes? Differences in the levels of job satisfaction and organizational commitment among managers in different countries are likely because these managers have different kinds of opportunities and rewards and because they face different economic, political, or sociocultural forces in their organizations' general environments. In countries with relatively high unemployment rates, such as France, levels of job satisfaction may be higher among employed managers because they may be happy simply to have a job.

Levels of organizational commitment from one country to another may depend on the extent to which countries have legislation affecting firings and layoffs and the extent to which citizens of a country are geographically mobile. In both France and Germany legislation protects workers (including managers) from being fired or laid off. U.S. workers, in contrast, have very little protection. In addition, managers in the United States are more willing to relocate than managers in France and



Research has shown that moods and emotions can affect worker motivation and performance. Positive moods may also enhance productivity, while negative moods may stifle it. What kinds of moods have you typically experienced on the job, and how have they affected your performance or that of others?

Figure 2.6
A Measure of
Organizational
Commitment

People respond to each of the items in the scale by checking whether they:

- | | |
|---|---|
| <input type="checkbox"/> Strongly disagree | <input type="checkbox"/> Slightly agree |
| <input type="checkbox"/> Moderately disagree | <input type="checkbox"/> Moderately agree |
| <input type="checkbox"/> Slightly disagree | <input type="checkbox"/> Strongly agree |
| <input type="checkbox"/> Neither disagree nor agree | |

- | | |
|--|--|
| _____ 1. I am willing to put in a great deal of effort beyond that normally expected in order to help this organization be successful. | _____ 9. It would take very little change in my present circumstances to cause me to leave this organization.* |
| _____ 2. I talk up this organization to my friends as a great organization to work for. | _____ 10. I am extremely glad that I chose this organization to work for over others I was considering at the time I joined. |
| _____ 3. I feel very little loyalty to this organization.* | _____ 11. There's not too much to be gained by sticking with this organization indefinitely.* |
| _____ 4. I would accept almost any type of job assignment in order to keep working for this organization. | _____ 12. Often, I find it difficult to agree with this organization's policies on important matters relating to its employees.* |
| _____ 5. I find that my values and the organization's values are very similar. | _____ 13. I really care about the fate of this organization. |
| _____ 6. I am proud to tell others that I am part of this organization. | _____ 14. For me this is the best of all possible organizations for which to work. |
| _____ 7. I could just as well be working for a different organization as long as the type of work was similar.* | _____ 15. Deciding to work for this organization was a definite mistake on my part.* |
| _____ 8. This organization really inspires the very best in me in the way of job performance. | |

Scoring: Responses to items 1, 2, 4, 5, 6, 8, 10, 13, and 14 are scored such that 1 = strongly disagree; 2 = moderately disagree; 3 = slightly disagree; 4 = neither disagree nor agree; 5 = slightly agree; 6 = moderately agree; and 7 = strongly agree. Responses to "****" items 3, 7, 9, 11, 12, and 15 are scored 7 = strongly disagree; 6 = moderately disagree; 5 = slightly disagree; 4 = neither disagree nor agree; 3 = slightly agree; 2 = moderately agree; and 1 = strongly agree. Responses to the 15 items are averaged for an overall score from 1 to 7; the higher the score, the higher the level of organizational commitment.

Source: L. W. Porter and F. J. Smith, "Organizational Commitment Questionnaire," in J. D. Cook, S. J. Hepworth, T. D. Wall, and P. B. Warr, eds., *The Experience of Work: A Compendium and Review of 249 Measures and Their Use* (New York: Academic Press, 1981), 84–86. Copyright © 1982, reprinted with permission of Elsevier.

Germany. In France citizens have relatively strong family and community ties; and in Germany housing is expensive and difficult to find. For those reasons citizens in both countries tend to be less geographically mobile than Americans.⁵³ Managers who know that their jobs are secure and who are reluctant to relocate (such as those in Germany and France) may be more committed to their organizations than managers who know that their organizations could lay them off any day and who would not mind geographic relocations.

Moods and emotions

mood A feeling or state of mind.

emotions Intense, relatively short-lived feelings.

Just as you sometimes are in a bad mood and at other times are in a good mood, so too are managers. A **mood** is a feeling or state of mind. When people are in a positive mood, they feel excited, enthusiastic, active, or elated.⁵⁴ When people are in a negative mood, they feel distressed, fearful, scornful, hostile, jittery, or nervous.⁵⁵ People who are high on extraversion are especially likely to experience positive moods; people who are high on negative affectivity are especially likely to experience negative moods. People's situations or circumstances also determine their moods; however, receiving a raise is likely to put most people in a good mood regardless of their personality traits. People who are high on negative affectivity are not always in a bad mood, and people who are low on extraversion still experience positive moods.⁵⁶

Emotions, more intense feelings than moods, are often directly linked to whatever caused the moods, and are more short-lived. However, once whatever has triggered the emotion has been dealt with, the feelings may linger in the form of a less intense mood.⁵⁷ For example, a manager who gets very angry when one of his subordinates has engaged in an unethical behavior may find his anger decreasing in intensity once he has decided how to address the problem. Yet he continues to be in a bad mood the rest of the day, even though he is not directly thinking about the unfortunate incident.⁵⁸

Research has found that moods and emotions affect the behavior of managers and all members of an organization. For example, research suggests that the subordinates of managers who experience positive moods at work may perform at somewhat higher levels and be less likely to resign and leave the organization than the subordinates of managers who do not tend to be in a positive mood at work.⁵⁹ Other research suggests that under certain conditions creativity might be enhanced by positive moods, whereas under other conditions negative moods might push people to work harder to come up with truly creative ideas.⁶⁰

Other research suggests that moods and emotions (which are more intense and short-lived feelings that are triggered by something specific) may play an important role in ethical decision making. For example, researchers at Princeton University found that when people are trying to solve difficult personal moral dilemmas, the parts of their brains that are responsible for emotions and moods are especially active.⁶¹

Recognizing the benefits of positive moods, the Northbrook, Illinois, accounting firm of Lipschultz, Levin, & Gray has gone to great lengths to promote positive feelings among its employees. Chief executive Steven Siegel claims that positive feelings promote relaxation and alleviate stress, increase revenues and attract clients, and reduce turnover. Positive moods are promoted in a variety of ways at Lipschultz, Levin, & Gray. Siegel has been known to put on a gorilla mask at especially busy times; clerks sometimes don chicken costumes; a foghorn announces the signing of a new client; employees can take a break and play miniature golf in the office, play darts, or exercise with a hula-hoop (even during tax time). A casual dress code also lightens things up at the firm. By all counts, positive moods seem to be paying off for this group of accountants, whose good feelings seem to be attracting new clients.

Patrick Corboy, president and chief executive of Austin Chemical, switched his account from a bigger firm to Lipschultz, Levin, & Gray because he found the people at the bigger firm to be "too stuffy and dour for us." Of the accountant William Finestone, who now manages the Austin Chemical account, Corboy says the following: "[He] is a barrel of laughs . . . Bill not only solves our problems more quickly but he puts us at ease, too."⁶²

Figure 2.7
A Measure of
Positive and
Negative Mood
at Work

People respond to each item by indicating the extent to which the item describes how they felt at work during the past week on the following scale:

- | | |
|---------------------------------|-----------------|
| 1 = Very slightly or not at all | 4 = Quite a bit |
| 2 = A little | 5 = Very much |
| 3 = Moderately | |

- | | |
|-------------------|---------------------|
| ___ 1. Active | ___ 7. Enthusiastic |
| ___ 2. Distressed | ___ 8. Fearful |
| ___ 3. Strong | ___ 9. Peppy |
| ___ 4. Excited | ___ 10. Nervous |
| ___ 5. Scornful | ___ 11. Elated |
| ___ 6. Hostile | ___ 12. Jittery |

Scoring: Responses to items 1, 3, 4, 7, 9, and 11 are summed for a positive mood score; the higher the score, the more positive mood is experienced at work. Responses to items 2, 5, 6, 8, 10, and 12 are summed for a negative mood score; the higher the score, the more negative mood is experienced at work.

Source: A. P. Brief, M. J. Burke, J. M. George, B. Robinson, and J. Webster, "Should Negative Affectivity Remain an Unmeasured Variable in the Study of Job Stress?" *Journal of Applied Psychology* 73 (1988), 193–198; M. J. Burke, A. P. Brief, J. M. George, L. Roberson, and J. Webster, "Measuring Affect at Work: Confirmatory Analyses of Competing Mood Structures with Conceptual Linkage in Cortical Regulatory Systems," *Journal of Personality and Social Psychology* 57 (1989), 1901–1102.

Nevertheless, sometimes negative moods can have their advantages. Some studies suggest that critical thinking and devil's advocacy may be promoted by a negative mood, and sometimes especially accurate judgments may be made by managers in negative moods.⁶³

Managers and other members of an organization need to realize that how they feel affects how they treat others and how others respond to them, including their subordinates. For example, a subordinate may be more likely to approach a manager with a somewhat far-out but potentially useful idea if the subordinate thinks the manager is in a good mood. Likewise, when managers are in very bad moods, their subordinates might try to avoid them at all costs. Figure 2.7 is an example of a scale that managers can use to measure the extent to which a person experiences positive and negative moods at work.

Emotional intelligence

emotional intelligence The ability to understand and manage one's own moods and emotions and the moods and emotions of other people.

In understanding the effects of managers' and all employees' moods and emotions, it is important to take into account their levels of emotional intelligence. **Emotional intelligence** is the ability to understand and manage one's own moods and emotions and the moods and emotions of other people.⁶⁴ Managers with a high level of emotional intelligence are more likely to understand how they are feeling and why, and they are more able to effectively manage their feelings. When managers are experiencing stressful feelings and emotions such as fear or anxiety, emotional intelligence enables them to understand why and manage these feelings so that they do not get in the way of effective decision making.⁶⁵

Emotional intelligence also can help managers perform their important roles such as their interpersonal roles (figurehead, leader, and liaison).⁶⁶ Understanding how your subordinates feel, why they feel that way, and how to manage these feelings is central to developing strong interpersonal bonds with them.⁶⁷ Moreover, emotional intelligence has the potential to contribute to effective leadership in multiple ways⁶⁸ and can help managers make lasting contributions to society, as profiled in the following “Manager as a Person.”



Manager as a Person

Bernie Goldhirsh's Legacy

Bernard (Bernie) Goldhirsh founded *INC.* magazine back in 1979, when entrepreneurs received more notoriety than respect, if they were paid attention to at all.⁶⁹ Goldhirsh was an entrepreneur himself at the time, with his own publishing company. He recognized the vast contributions entrepreneurs could make to society, creating something out of nothing, and also realized firsthand what a tough task entrepreneurs faced.⁷⁰ His emotional intelligence helped him to understand the challenges and frustrations entrepreneurs like himself faced and their need for support.

When Goldhirsh founded *INC.*, entrepreneurs had little they could turn to for advice, guidance, and solutions to management problems. *INC.* was born to fill this gap and provide entrepreneurs with information and support by profiling successful and unsuccessful entrepreneurial ventures, highlighting management techniques that work, and providing readers with firsthand accounts of how successful entrepreneurs developed and managed their businesses.⁷¹

Goldhirsh had an inquisitive mind and liked to go where his thoughts and conversations took him. Although he founded *INC.* magazine and inspired his staff, he let his writers and editors have free rein with the magazine's content. They were the experts he chose to write and edit the magazine, and he realized it was not his place to interfere with editorial matters. What he did do, and do very well, was inspire his staff to be enthusiastic about the mission of *INC.* and the role of the entrepreneur as a self-reliant explorer, going off into the unknown. As Goldhirsh put it, entrepreneurs create new businesses “from nothing, just blank canvas. . . . It's amazing. Somebody goes into a garage, has nothing but an idea, and out of the garage comes a company, a living company. It's so special what they do. They are a treasure.”⁷²

Goldhirsh's emotional intelligence helped him recognize the many barriers entrepreneurs face and the emotional roller coaster of staking all one has on an idea that may or may not work. Goldhirsh believed that helping society understand the entrepreneurial process through *INC.* magazine not only helped entrepreneurs but also enlightened bankers, lawmakers, and the public at large about the role these visionaries play, the challenges they face, and the support their ventures depend on.⁷³

When Goldhirsh was diagnosed with brain cancer at age 60, he sold *INC.* magazine at the urging of his doctors. From the proceeds of the sale, he distributed \$20 million to *INC.*'s employees, and he dedicated \$50 million to a foundation supporting brain cancer research. Goldhirsh inspired *INC.*'s employees to recognize that the magazine had only gotten started and had an important and growing future ahead, and this has certainly been the case.⁷⁴ It was a sad day at *INC.* when Goldhirsh passed away but also an opportunity to reflect on the ongoing contributions of a man who saw the ultimate good in entrepreneurship and whose efforts to support it live on today through the magazine he founded.⁷⁵

Figure 2.8
A Measure of Emotional Intelligence

Scoring: Self-emotions appraisal = sum of items 1, 5, 9, 13
Others-emotions appraisal = sum of items 2, 6, 10, 14
Use of emotion = sum of items 3, 7, 11, 15
Regulation of emotion = sum of items 4, 8, 12, 16

Source: K. Law, C. Wong, and L. Song, "The Construct and Criterion Validity of Emotional Intelligence and Its Potential Utility for Management Studies," *Journal of Applied Psychology* 89, no. 3 (2004), 496; C. S. Wong and K. S. Law, "The Effects of Leader and Follower Emotional Intelligence on Performance and Attitude: An Exploratory Study," *Leadership Quarterly* 13 (2002), 243-274.

Organizational Culture

organizational culture

The shared set of beliefs, expectations, values, norms, and work routines that influence the ways in which individuals, groups, and teams interact with one another and cooperate to achieve organizational goals.

Personality is a way of understanding why all managers and employees, as individuals, characteristically think and behave in different ways. However, when people belong to the same organization, they often tend to share certain beliefs and values that lead them to act in similar ways.⁸⁰ **Organizational culture** comprises the shared set of beliefs, expectations, values, norms, and work routines that influence how members of an organization relate to one another and work together to achieve organizational goals. In essence, organizational culture reflects the distinctive ways organizational members go about performing their jobs and relating to others inside and outside the organization. It may, for example, be a distinctive way in which customers in a particular hotel chain are treated from the time they are greeted at check-in until their stay is completed; or it may be the shared work routines that research teams use to guide new product development. When organizational members share an intense commitment to cultural values, beliefs, and routines and use them to achieve their goals, a *strong* organizational culture exists. When organizational members are not strongly committed to a shared system of values, beliefs, and routines, organizational culture is weak.

The stronger the culture of an organization, the more one can think about it as being the “personality” of an organization because it influences the way its members behave.⁸¹ Organizations that possess strong cultures may differ on a wide variety of dimensions that determine how their members behave toward one another and perform their jobs. For example, organizations differ in terms of how members relate to each other (e.g., formally or informally), how important decisions are made (e.g., top-down or bottom-up), willingness to change (e.g., flexible or unyielding), innovation (e.g., creative or predictable), and playfulness (e.g., serious or serendipitous). In an innovative design firm like IDEO Product Development in Silicon Valley, employees are encouraged to adopt a playful attitude to their work, look outside the organization to find inspiration, and adopt a flexible approach toward product design that uses multiple perspectives.⁸² IDEO’s culture is vastly different from that of companies such as Citibank and ExxonMobil, in which employees treat each other in a more formal or deferential way, employees are expected to adopt a serious approach to their work, and decision making is constrained by the hierarchy of authority.

Managers and organizational culture

While all members of an organization can contribute to the development and maintenance of organizational culture, managers play a particularly important part in influencing organizational culture,⁸³ given their multiple and important roles (see Chapter 1). How managers create culture is most vividly evident in start-ups of new companies. Entrepreneurs who start their own companies are typically also the start-ups’ top managers until the companies grow and/or become profitable. Often referred to as the firms’ founders, these managers literally create their organizations’ cultures.

Often, the founders’ personal characteristics play an important role in the creation of organizational culture. Benjamin Schneider, a well-known management researcher, developed a model that helps to explain the role that founders’ personal characteristics play in determining organizational culture.⁸⁴ His model, called the **attraction-selection-attrition (ASA) framework**, posits that when founders hire

attraction-

selection-attrition (ASA) framework

A model that explains how personality may influence organizational culture.

employees for their new ventures, they tend to be attracted to and choose employees whose personalities are similar to their own.⁸⁵ These similar employees are more likely to stay with the organization. While employees who are dissimilar in personality might be hired, they are more likely to leave the organization over time.⁸⁶ As a result of these attraction, selection, and attrition processes, people in the organization tend to have similar personalities, and the typical or dominant personality profile of organizational members determines and shapes organizational culture.⁸⁷

For example, when David Kelley became interested in engineering and product design challenges in the late 1970s, he realized that who he was as a person meant that he would not be happy working in the typical corporate environment. Kelley is high on openness to experience, driven to go where his interests take him, and not content to follow others' directives. Kelley recognized that he needed to start his own business and, with the help of other Stanford-schooled engineers and design experts, IDEO was born.⁸⁸

From the start, IDEO's culture has embodied Kelley's spirited, freewheeling approach to work and design—from colorful and informal work spaces to an emphasis on networking and communicating with as many people as possible to understand a design problem. No project or problem is too big or too small for IDEO: The company designed the Apple Lisa computer and mouse (the precursor of the Mac) and the Palm as well as the Crest Neat Squeeze toothpaste dispenser and the Racer's Edge water bottle. Kelley hates rules, job titles, big corner offices, and all the other trappings of large traditional organizations that stifle creativity. Employees who are attracted to, selected by, and remain with IDEO value creativity and innovation and embrace one of IDEO's mottos: "Fail often to succeed sooner."⁸⁹

While ASA processes are most evident in small firms such as IDEO, they also can operate in large companies.⁹⁰ According to the ASA model, this is a naturally occurring phenomenon to the extent that managers and new hires are free to make the kinds of choices the model specifies. While people tend to get along well with others who are similar to themselves, too much similarity in an organization can actually impair organizational effectiveness. That is, similar people tend to view

conditions and events in similar ways and thus can be resistant to change. Moreover, organizations benefit from a diversity of perspectives rather than similarity in perspectives (see Chapter 4). At IDEO, Kelley recognized early on how important it is to take advantage of the diverse talents and perspectives that people with different personalities, backgrounds, experiences, and education can bring to a design team. Hence, IDEO's design teams include not only engineers but others who might have a unique insight into a problem, such as anthropologists, communications experts, doctors, and users of a product. When new employees are hired at IDEO, they meet with many employees who have different backgrounds and characteristics—the focus is not on hiring someone who will “fit in” but, rather, on hiring someone who has something to offer and can “wow” different kinds of people with his or her insights.⁹¹



An IDEO team works on a project. IDEO designed many products we take for granted, such as the first Apple mouse and stand-up toothpaste containers. IDEO's “playful” culture goes hand-in-hand with the creative nature of its products and services.

In addition to personality, other personal characteristics of managers shape organizational culture; these include managers' values, attitudes, moods and emotions, and emotional intelligence.⁹² For example, both terminal and instrumental values of managers play a role in determining organizational culture. Managers who highly value freedom and equality, for example, might be more likely to stress the importance of autonomy and empowerment in their organizations, as well as fair treatment for all. As another example, managers who highly value being helpful and forgiving may not only be tolerant of mistakes but also be prone to emphasize the importance of organizational members' being kind and helpful to one another.

Managers who are satisfied with their jobs, are committed to their organizations, and experience positive moods and emotions might also encourage these attitudes and feelings in others. The result would be an organizational culture emphasizing positive attitudes and feelings. Research suggests that attitudes like job satisfaction and organizational commitment can be affected by the influence of others. Managers are in a particularly strong position to engage in social influence given their multiple roles. Moreover, research suggests that moods and emotions can be "contagious" and that spending time with people who are excited and enthusiastic can increase one's own levels of excitement and enthusiasm.

The role of values and norms in organizational culture

Shared terminal and instrumental values play a particularly important role in organizational culture. *Terminal values* signify what an organization and its employees are trying to accomplish, and *instrumental values* guide the ways in which the organization and its members achieve organizational goals. In addition to values, shared norms also are a key aspect of organizational culture. Recall that norms are unwritten, informal rules or guidelines that prescribe appropriate behavior in particular situations. For example, norms at IDEO include not being critical of others' ideas, coming up with multiple ideas before settling on one, and developing prototypes of new products.⁹³

Managers determine and shape organizational culture through the kinds of values and norms they promote in an organization. Some managers, like David Kelley of IDEO, cultivate values and norms that encourage risk taking, creative responses to problems and opportunities, experimentation, tolerance of failure in order to succeed, and autonomy.⁹⁴ Top managers at organizations such as Intel, Microsoft, and Sun Microsystems encourage employees to adopt such values to support their commitment to innovation as a source of competitive advantage.

Other managers, however, might cultivate values and norms that indicate to employees that they should always be conservative and cautious in their dealings with others and should try to consult with their superiors before making important decisions or any changes to the status quo. Accountability for actions and decisions is stressed, and detailed records are kept to ensure that policies and procedures are followed. In settings where caution is needed—nuclear power stations, large oil refineries, chemical plants, financial institutions, insurance companies—a conservative, cautious approach to making decisions might be highly appropriate.⁹⁵ In a nuclear power plant, for example, the catastrophic consequences of a mistake make a high level of supervision vital. Similarly, in a bank or mutual fund company, the risk of losing investors' money makes a cautious approach to investing highly appropriate.

Figure 2.9
Factors That
Maintain and
Transmit
Organizational
Culture



Managers of different kinds of organizations deliberately cultivate and develop the organizational values and norms that are best suited to their task and general environments, strategy, or technology. Organizational culture is maintained and transmitted to organizational members through the values of the founder, the process of socialization, ceremonies and rites, and stories and language (see Figure 2.9).

VALUES OF THE FOUNDER From the ASA model discussed above, it is clear that founders of an organization can have profound and long-lasting effects on organizational culture. Founders' values inspire them to start their own companies and, in turn, drive the nature of these new companies and their defining characteristics. Thus, the terminal and instrumental values of an organization's founder have a substantial influence on the values, norms, and standards of behavior that develop over time within the organization.⁹⁶ Founders set the scene for the way cultural values and norms develop because their own values guide the building of the company and they hire other managers and employees who the founder believes will share these values and help the organization to attain them. Moreover, new managers quickly learn from the founder what values and norms are appropriate in the organization and thus what is desired of them. Subordinates imitate the style of the founder and, in turn, transmit their values and norms to their subordinates. Gradually, over time, the founder's values and norms permeate the organization.⁹⁷

A founder who requires a great display of respect from subordinates and insists on proprieties such as formal job titles and formal modes of dress encourages subordinates to act in this way toward their subordinates. Often, a founder's personal values affect an organization's competitive advantage. For example, McDonald's founder Ray Kroc insisted from the beginning on high standards of customer service and cleanliness at McDonald's restaurants; these became core sources of McDonald's competitive advantage. Similarly, Bill Gates, the founder of Microsoft, pioneered certain cultural values in Microsoft. Employees are expected to be creative and to work hard, but they are encouraged to dress informally and to personalize their offices. Gates also established a host of company events such as cookouts, picnics, and sports events to emphasize to employees the importance of being both an individual and a team player.

SOCIALIZATION Over time, organizational members learn from each other which values are important in an organization and the norms that specify appropriate and inappropriate behaviors. Eventually, organizational members behave in accordance with the organization's values and norms—often without realizing they

organizational socialization

The process by which newcomers learn an organization's values and norms and acquire the work behaviors necessary to perform jobs effectively.

are doing so. **Organizational socialization** is the process by which newcomers learn an organization's values and norms and acquire the work behaviors necessary to perform jobs effectively.⁹⁸ As a result of their socialization experiences, organizational members internalize an organization's values and norms and behave in accordance with them not only because they think they have to but because they think that these values and norms describe the right and proper way to behave.⁹⁹

At Texas A&M University, for example, all new students are encouraged to go to "Fish Camp" to learn how to be an "Aggie" (the traditional nickname of students at the university). They learn about the ceremonies that have developed over time to commemorate significant events or people in A&M's history. In addition, they learn how to behave at football games and in class and what it means to be an Aggie. As a result of this highly organized socialization program, by the time new students arrive on campus and start their first semester, they have been socialized into what a Texas A&M student is supposed to do, and they have relatively few problems adjusting to the college environment.

Most organizations have some kind of socialization program to help new employees learn the ropes—the values, norms, and culture of the organization. The military, for example, is well known for the rigorous socialization process it uses to turn raw recruits into trained soldiers. Organizations such as the Walt Disney Company also put new recruits through a rigorous training program to provide them with the knowledge they need not only to perform well in their jobs but also to ensure that each employee plays his or her part in helping visitors to Disneyland have fun in a wholesome theme park. New recruits at Disney are called "cast members" and attend Disney University to learn the Disney culture and their part in it. Disney's culture emphasizes the values of safety, courtesy, entertainment, and efficiency, and these values are brought to life for newcomers at Disney University.



Texas A&M's Fish Camp is an annual orientation program designed to help freshmen (or Fish) make the transition from high school to college life. Texas A&M's Fish Camp runs for four days and is attended by over 4,500 freshmen each year.

Table 2.1
Organizational Rites

Type of Rite	Example of Rite	Purpose of Rite
Rite of passage	Induction and basic training	Learn and internalize norms and values
Rite of integration	Office Christmas party	Build common norms and values
Rite of enhancement	Presentation of annual award	Motivate commitment to norms and values

Newcomers also learn about the attraction area they will be joining (e.g., Adventureland or Fantasyland) at Disney University and then receive on-the-job socialization in the area itself from experienced cast members.¹⁰⁰ Through organizational socialization, founders and managers of an organization transmit to employees the cultural values and norms that shape the behavior of organizational members. Thus, the values and norms of founder Walt Disney live on today at Disneyland as newcomers are socialized into the Disney way.

CEREMONIES AND RITES Another way in which managers can create or influence organizational culture is by developing organizational *ceremonies and rites*—formal events that recognize incidents of importance to the organization as a whole and to specific employees.¹⁰¹ The most common rites that organizations use to transmit cultural norms and values to their members are rites of passage, of integration, and of enhancement (see Table 2.1).¹⁰²

Rites of passage determine how individuals enter, advance within, or leave the organization. The socialization programs developed by military organizations (such as the U.S. Army) or by large accountancy and law firms are rites of passage. Likewise, the ways in which an organization prepares people for promotion or retirement are rites of passage.

Rites of integration, such as shared announcements of organizational successes, office parties, and company cookouts, build and reinforce common bonds among organizational members. IDEO uses many rites of integration to make its employees feel connected to one another and special. In addition to having wild “end-of-year” celebratory bashes, groups of IDEO employees periodically take time off to go to a sporting event, movie, or meal or, sometimes, on a long bike ride or sail. These kinds of shared activities not only reinforce IDEO’s culture but also can be a source of inspiration on the job (e.g., IDEO has been involved in the making of movies such as *The Abyss* and *Free Willy*). One 35-member design studio at IDEO led by Dennis Boyle has bimonthly lunch fests with no set agenda—anything goes. While enjoying great food, jokes, and camaraderie, studio members often end up sharing ideas for their latest great products, and the freely flowing conversation that results often leads to creative insights.¹⁰³

A company’s annual meeting also may be used as a ritual of integration, offering an opportunity to communicate organizational values to managers, other employees, and shareholders. Wal-Mart, for example, makes its annual stockholders’ meeting an extravagant ceremony that celebrates the company’s success. The company often flies thousands of its highest-performing employees to its annual meeting at its Bentonville, Arkansas, headquarters for a huge weekend entertainment festival



Wal-Mart managers attending an annual meeting in Kansas City, Missouri. Wal-Mart believes that entertainment reinforces its high-performance culture and values. These events, or “rites of integration,” reinforce common bonds among members of an organization.

complete with performances by country and western stars. Wal-Mart believes that rewarding its supporters with entertainment reinforces the company’s high-performance values and culture. The proceedings are shown live over closed-circuit television in all Wal-Mart stores so that all employees can join in the rites celebrating the company’s achievements.¹⁰⁴

Rites of enhancement, such as awards dinners, newspaper releases, and employee promotions, let organizations publicly recognize and reward employees’ contributions and thus strengthen their commitment to organizational values. By bonding members within the organization, rites of enhancement reinforce an organization’s values and norms.

Stories and language also communicate organizational culture. Stories (whether fact or fiction) about organizational heroes and villains and their actions provide important clues about values and norms. Such stories can reveal the kinds of behaviors that are valued by the organization and the kinds of practices that are frowned on.¹⁰⁵ At the heart of McDonald’s rich culture are hundreds of stories that organizational members tell about founder Ray Kroc. Most of these stories focus on how Kroc established the strict operating values and norms that are at the heart of McDonald’s culture. Kroc was dedicated to achieving perfection in McDonald’s quality, service, cleanliness, and value for money (QSC&V), and these four central values permeate McDonald’s culture. For example, an often retold story describes what happened when Kroc and a group of managers from the Houston region were touring various restaurants. One of the restaurants was having a bad day operationally. Kroc was incensed about the long lines of customers, and he was furious when he realized that the product customers were receiving that day was not up to his high standards. To address the problem, he jumped up and stood on the front counter and got the attention of all customers and operating crew personnel. He introduced himself, apologized for the long wait and cold food, and told the customers that they could have freshly cooked food or their money back—whichever they wanted. As a result, the customers left happy, and when Kroc checked on the restaurant later, he found that his message had gotten through to its managers and crew—performance had improved. Other stories describe Kroc scrubbing dirty toilets and picking up litter inside or outside a restaurant. These and similar stories are spread around the organization by McDonald’s employees. They are the stories that have helped establish Kroc as McDonald’s “hero.”

Because spoken language is a principal medium of communication in organizations, the characteristic slang or jargon—that is, organization-specific words or phrases—that people use to frame and describe events provides important clues about norms and values. “McLanguage,” for example, is prevalent at all levels of McDonald’s. A McDonald’s employee described as having “ketchup in his (or her) blood” is someone who is truly dedicated to the McDonald’s way—someone who

has been completely socialized to its culture. McDonald's has an extensive training program that teaches new employees "McDonald's speak," and new employees are welcomed into the family with a formal orientation that illustrates Kroc's dedication to QSC&V.

The concept of organizational language encompasses not only spoken language but how people dress, the offices they occupy, the cars they drive, and the degree of formality they use when they address one another. Casual dress reflects and reinforces Microsoft's entrepreneurial culture and values. Formal business attire supports the conservative culture found in many banks, which emphasize the importance of conforming to organizational norms such as respect for authority and staying within one's prescribed role. Traders in the Chicago futures and options trading pits frequently wear garish and flamboyant ties and jackets to make their presence known in a sea of faces. The demand for magenta, lime green, and silver lamé jackets featuring bold images such as the Power Rangers—anything that helps the traders stand out and attract customers—is enormous.¹⁰⁶ When employees speak and understand the language of their organization's culture, they know how to behave in the organization and what is expected of them.

At IDEO, language, dress, the physical work environment, and extreme informality all underscore a culture that is adventuresome, playful, risk-taking, egalitarian, and innovative. For example, at IDEO, employees refer to taking the consumers' perspective when designing products as "being left-handed." Employees dress in T-shirts and jeans, the physical work environment is continually evolving and changing depending upon how employees wish to personalize their workspace, no one "owns" a fancy office with a window, and rules are nonexistent.¹⁰⁷

Culture and managerial action

While founders and managers play a critical role in the development, maintenance, and communication of organizational culture, this same culture shapes and controls the behavior of all employees, including managers themselves. For example, culture influences the way managers perform their four main functions: planning, organizing, leading, and controlling. As we consider these functions, we continue to distinguish between top managers who create organizational values and norms that encourage creative, innovative behavior and top managers who encourage a conservative, cautious approach by their subordinates. We noted earlier that both kinds of values and norms can be appropriate depending upon the situation and type of organization.

PLANNING Top managers in an organization with an innovative culture are likely to encourage lower-level managers to participate in the planning process and develop a flexible approach to planning. They are likely to be willing to listen to new ideas and to take risks involving the development of new products. In contrast, top managers in an organization with conservative values are likely to emphasize formal top-down planning. Suggestions from lower-level managers are likely to be subjected to a formal review process, which can significantly slow decision making. Although this deliberate approach may improve the quality of decision making in a nuclear power plant, it can have unintended consequences. In the past, at conservative IBM, the planning process became so formalized that managers spent most of their time assembling complex slide shows and overheads to defend their current positions rather than thinking about what they should be doing to keep IBM abreast of the changes taking place in the computer industry. When former

CEO Lou Gerstner took over, he used every means at his disposal to abolish this culture, even building a brand-new campus-style headquarters to change managers' mind-sets. As indicated in the earlier IT Byte, IBM's culture is undergoing further changes initiated by its new CEO, Samuel Palmisano.

ORGANIZING What kinds of organizing will managers in innovative and in conservative cultures encourage? Valuing creativity, managers in innovative cultures are likely to try to create an organic structure, one that is flat, with few levels in the hierarchy, and one in which authority is decentralized so that employees are encouraged to work together to find solutions to ongoing problems. A product team structure may be very suitable for an organization with an innovative culture. In contrast, managers in a conservative culture are likely to create a well-defined hierarchy of authority and establish clear reporting relationships so that employees know exactly whom to report to and how to react to any problems that arise.

LEADING In an innovative culture, managers are likely to lead by example, encouraging employees to take risks and experiment. They are supportive regardless of whether employees succeed or fail. In contrast, managers in a conservative culture are likely to use management by objectives and to constantly monitor subordinates' progress toward goals, overseeing their every move. We examine leadership in detail in Chapter 10 when we consider the leadership styles that managers can adopt to influence and shape employee behavior.

CONTROLLING The ways in which managers evaluate and take actions to improve performance differ depending upon whether the organizational culture emphasizes formality and caution or innovation and change. Managers who want to encourage risk-taking, creativity, and innovation recognize that there are multiple potential paths to success and that failure must be accepted in order for creativity to thrive. Thus, they are less concerned about employees' performing their jobs in a specific, predetermined manner and in strict adherence to preset goals and more concerned about employees' being flexible and taking the initiative to come up with ideas for improving performance. Managers in innovative cultures are also more concerned about long-run performance than short-term targets because they recognize that real innovation entails much uncertainty that necessitates flexibility. In contrast, managers in cultures that emphasize caution and maintenance of the status quo often set specific, difficult goals for employees, frequently monitor progress toward these goals, and develop a clear set of rules that employees are expected to adhere to.

The values and norms of an organization's culture strongly affect the way managers perform their management functions. The extent to which managers buy into the values and norms of their organization shapes their view of the world and their actions and decisions in particular circumstances.¹⁰⁸ In turn, the actions that managers take can have an impact on the performance of the organization. Thus, organizational culture, managerial action, and organizational performance are all linked together.

This linkage is apparent at Hewlett-Packard (HP), a leader in the electronic instrumentation and computer industries. Established in the 1940s, HP developed a culture that is an outgrowth of the strong personal beliefs of the company's founders, William Hewlett and David Packard. Bill and Dave, as they are known within the company, formalized HP's culture in 1957 in a statement of corporate objectives known as the "HP Way." The basic values informing the HP Way stress serving everyone who has a stake in the company with integrity and fairness,

including customers, suppliers, employees, stockholders, and society in general. Bill and Dave helped build this culture within HP by hiring like-minded people and by letting the HP Way guide their own actions as managers.

Although the Hewlett-Packard example and our earlier example of IDEO illustrate how organizational culture can give rise to managerial actions that ultimately benefit the organization, this is not always the case. The cultures of some organizations become dysfunctional, encouraging managerial actions that harm the organization and discouraging actions that might lead to an improvement in performance.¹⁰⁹ Recent corporate scandals at large companies like Enron, Tyco, and WorldCom show how damaging a dysfunctional culture can be to an organization and its members. For example, Enron's arrogant, "success-at-all costs" culture led to fraudulent behavior on the part of its top managers.¹¹⁰ Unfortunately, hundreds of Enron employees have paid a heavy price for the unethical behavior of these top managers and the dysfunctional organizational culture. Not only have these employees lost their jobs, but many also have lost their life savings in Enron stock and pension funds, which became worth just a fraction of their former value before the wrongdoing at Enron came to light. We discuss ethics in depth in the next chapter.

Summary and Review

ENDURING CHARACTERISTICS: PERSONALITY TRAITS

Personality traits are enduring tendencies to feel, think, and act in certain ways. The Big Five general traits are extraversion, negative affectivity, agreeableness, conscientiousness, and openness to experience. Other personality traits that affect managerial behavior are locus of control, self-esteem, and the needs for achievement, affiliation, and power.

VALUES, ATTITUDES, AND MOODS AND EMOTIONS

A terminal value is a personal conviction about lifelong goals or objectives; an instrumental value is a personal conviction about modes of conduct. Terminal and instrumental values have an impact on what managers try to achieve in their organizations and the kinds of behaviors they engage in. An attitude is a collection of feelings and beliefs. Two attitudes important for understanding managerial behaviors include job satisfaction (the collection of feelings and beliefs that managers have about their jobs) and organizational commitment (the collection of feelings and beliefs that managers have about their organizations). A mood is a feeling or state of mind; emotions are intense feelings that are short-lived and directly linked to their causes. Managers' moods and emotions, or how they feel at work on a day-to-day basis, have the potential to impact not only their own behavior and effectiveness but also those of their subordinates. Emotional intelligence is the ability to understand and manage one's own and other people's moods and emotions.

ORGANIZATIONAL CULTURE Organizational culture is the shared set of beliefs, expectations, values, norms, and work routines that influence how members of an organization relate to one another and work together to achieve organizational goals. Founders of new organizations and managers play an important role in creating and maintaining organizational culture. Organizational socialization is the process by which newcomers learn an organization's values and norms and acquire the work behaviors necessary to perform jobs effectively.



Management in Action

Topics for Discussion and Action

Discussion

1. Discuss why managers who have different types of personalities can be equally effective and successful.
2. Can managers be too satisfied with their jobs? Can they be too committed to their organizations? Why or why not?
3. Assume that you are a manager of a restaurant. Describe what it is like to work for you when you are in a negative mood.
4. Why might managers be disadvantaged by low levels of emotional intelligence?

Action

5. Interview a manager in a local organization. Ask the manager to describe situations in which he or she is especially likely to act in accordance with his or her values. Ask the manager to describe situations in which he or she is less likely to act in accordance with his or her values.
6. Watch a popular television show, and as you watch it, try to determine the emotional intelligence levels of the characters the actors in the show portray. Rank the characters from highest to

lowest in terms of emotional intelligence. As you watched the show, what factors influenced your assessments of emotional intelligence levels?

7. Go to an upscale clothing store in your neighborhood, and go to a clothing store that is definitely not upscale. Observe the behavior of employees in each store as well as the store's environment. In what ways are the organizational cultures in each store similar? In what ways are they different?



Building Management Skills

Think about the culture of the last organization you worked for, your current university, or another organization or club to which you belong. Then, answer the following questions:

1. What values are emphasized in this culture?
2. What norms do members of this organization follow?
3. Who seems to have played an important role in creating the culture?
4. In what ways is the organizational culture communicated to organizational members?

Diagnosing Culture





Small Group Breakout Exercise

Making Difficult Decisions in Hard Times

Form groups of three or four people, and appoint one member as the spokesperson who will communicate your findings to the whole class when called on by the instructor. Then discuss the following scenario.

You are on the top-management team of a medium-size company that manufactures cardboard boxes, containers, and other cardboard packaging materials. Your company is facing increasing levels of competition for major corporate customer accounts, and profits have declined significantly. You have tried everything you can to cut costs and remain competitive, with the exception of laying off employees. Your company has had a no-layoff policy for the past 20 years, and you believe it is an

important part of the organization's culture. However, you are experiencing mounting pressure to increase your firm's performance, and your no-layoff policy has been questioned by shareholders. Even though you haven't decided whether to lay off employees and thus break with a 20-year tradition for your company, rumors are rampant in your organization that something is afoot, and employees are worried. You are meeting today to address this problem.

1. Develop a list of options and potential courses of action to address the heightened competition and decline in profitability that your company has been experiencing.
2. Choose your preferred course of action, and justify why you will take this route.
3. Describe how you will communicate your decision to employees.
4. If your preferred option involves a layoff, justify why. If it doesn't involve a layoff, explain why.



Be the Manager

You have recently been hired as the vice president for human resources in an advertising agency. One of the problems that has been brought to your attention is the fact that in the creative departments at the agency, there are dysfunctionally high levels of conflict. You have spoken with members of each of

these departments, and in each one it seems that there are a few members of the department who are creating all the problems. All of these individuals are valued contributors who have many creative ad campaigns to their credit. The very high levels of conflict are creating problems in the departments, and

negative moods and emotions are much more prevalent than positive feelings. What are you going to do to both retain valued employees and alleviate the excessive conflict and negative feelings in these departments?



Managing Ethically

Some organizations rely on personality and interest inventories to screen potential employees. Other organizations attempt to screen employees by using paper-and-pencil honesty tests.

personality and interest inventories to screen potential employees. How might this practice be unfair to potential applicants? How might organizational members who are in charge of hiring misuse it?

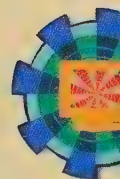
people may "fail" an honesty test given by an employer. What are the ethical implications of trustworthy people "failing" honesty tests, and what obligations do you think employers should have when relying on honesty tests for screening purposes?

Questions

1. Either individually or in a group, think about the ethical implications of using
2. Because of measurement error and validity problems, some relatively trustworthy

Additional Activities on the Build Your Management Skills DVD

- **Test Your Knowledge:** Types, Causes, and Management of Stress
- **Self-Assessment:** (1) Assessing Your Emotional Intelligence; (2) Corporate Cultures Preferences Scale; (3) Type "A" Scale; and
- (4) What Is Your Level of Self-Esteem?
- **Manager's Hot Seat:** Personal Disclosure: Confession Coincidence



BusinessWeek

Case in the News

The Wizard of Odd

Wackiness is grocer Jim Bonaminio's calling card. Will he keep Wal-Mart at bay?

James O. Bonaminio is an independent grocer with a capital "I." Today, if the mood strikes, Bonaminio might put on his wizard suit and roller-skate through his Jungle Jim's International Market performing "price magic." Or perhaps he'll go off "junking" for a few hours, returning with a ton or two of bargain-priced salvage that he eventually will incorporate into his sprawling, 280,000-square-foot supermarket in Fairfield, Ohio—just like he did with the animatronic Robin Hood, the 40,000 blocks of wood extracted from highway guardrails, and the monorail recycled from an amusement-park ride.

Jungle Jim's might well be America's wackiest supermarket, but there is method to Bonaminio's madeness. Instead of trying to beat the big chains at their price-squeezing game, Bonaminio has built a funhouse maze of a store north of Cincinnati that draws 50,000 shoppers a week from as far away as Indianapolis and Lexington, Ky. "The Jungle" is not all fun and frivolity; its other defining

trait is a huge selection of specialty foods from 75 countries. Sales totaled \$63.5 million in 2004, up from \$29.8 million in 1995—not bad for a college dropout who got his start in 1971 selling produce from a roadside stand. (Bonaminio says he turns a profit, but he won't disclose numbers.)

Jungle Jim's is as unique as a fingerprint, but it typifies retailing today in one respect: Its future is threatened by the relentless expansion of Wal-Mart Stores Inc. "People say, 'don't worry about Wal-Mart, you are unique.' "[But] Independents are different, man; you can't ever let your guard down."

Wal-Mart has been slow to move into Cincinnati, in part because the city is home to Kroger Co., the largest U.S. supermarket chain. Last September, though, the discounter opened the first of what is expected to be about 15 megastores ringing Cincinnati. "I see Wal-Mart going from nothing to a 25 percent to 30 percent market share in four years," says David B. Birdsall, the Midwestern develop-

ment chief of Regency Centers Corp., which owns a dozen shopping centers in greater Cincinnati, including one that is anchored by that just-completed Wal-Mart Supercenter.

Slowing Growth

Kroger, Meijer, Bigg's, and Cincinnati's other established grocers are about two years into a fierce struggle to try to add market share before Wal-Mart starts taking it away. Jungle Jim's dual emphasis on shopping-as-entertainment and specialty foods has insulated it from the price wars, but only to a degree. While Bonaminio makes most of his profit on high-margin specialty foods, he derives the bulk of his revenue from the same staples that every supermarket offers. Jungle Jim's growth has slowed markedly of late. Revenues have risen by 3.8 percent a year on average since 2002, compared with 11.4 percent from 1995 through 2001.

The looming prospect of being sandwiched between two Wal-Mart Supercenters about 10 miles apart

has roused Bonaminio to bold action. He is risking much of the profit he has accumulated on a \$10 million project to transform his store into a retail campus he calls "Foodieland." And on Apr. 1, Bonaminio signed a letter of intent to open a second store. The 75,000 sq. ft. supermarket—tentatively named Baby Jungle—will be a 30-minute drive from the Fairfield store, moving Bonaminio close to the heart of Cincinnati.

Jungle Jim's has prospered to date not because of its location but despite it, in defiance of the first rule of retailing. The store is four miles from the nearest major highway, and a long stretch of traffic hell separates it from Cincinnati proper. Even so, Bonaminio never seriously considered relocating even as his business began to expand.

His store is an amalgam of a dozen buildings constructed one after the other and joined together under one very complicated roof. Built largely of recycled materials, Jungle Jim's is filled with novel design touches that Bonaminio delights in showing off: the antique fire engine resting atop a case holding 1,200 kinds of hot sauce; the mint-condition 1919 Boar's Head truck in the deli section; the faux Portopotty doors that open into spacious bathrooms; and on and on.

Bonaminio put his Foodieland plan in motion a few years ago, and it is about half realized. Next to the store he recently built a two-story "events center" for tastings, televised cooking demonstrations, and food and wine festivals. Within the new building is a large space that Bonaminio hopes to let to a restaurant operator. He's also looking to lure a hotel chain to his 71-acre

property. "There are golf destinations all over America where you fly in and spend the weekend," Bonaminio says. "That's what I'm trying to do with Foodieland—create a campus with things for foodies to do when they're not shopping the store."

Plants, Stamps, Latte

Bonaminio also is counting on the allure of one-stop shopping to ring the cash register. He has added a garden center outside the front entrance and leased space just inside it to a U. S. Post Office, a Fifth Third Bank branch, a Starbucks, and a pharmacy. Bonaminio just broke ground on a shopping center next to the Jungle with room for a dozen restaurants and stores. Most of its 65,000 square feet already have been leased. "Such a huge number of people come through Jungle Jim's that if we just pick off 10 percent of them, we will make money hand over first," says Brian Gillan, CEO of Buck\$ Dollar Stores, a small Cincinnati chain.

Foodieland's most distinctive feature—a two-mile monorail—will connect the far reaches of Jungle Jim's parking lot to various entrances when it begins operating in 2006. Bonaminio picked up eight trains from an area amusement park for just \$1 in 1998 but has spent \$1 million upgrading them and installing track. Part of what finally persuaded him to open a second store was the change to adapt an old machine-tool warehouse for retail use. With the building comes a secondhand treasure to rival the monorail: a 25-ton crane. It's staying.

The consensus in Cincinnati retailing and real estate circles is

that Wal-Mart's inevitable market share gains are unlikely to come at Bonaminio's expense. "Jungle seems wacky on the outside, but he has a consumer brilliance about him," says Robert Smyjunas Jr., president of Cincinnati developer Vandercar Holdings Inc., which has been trying for years to entice Bonaminio into one of its projects. "He really understand his market."

For his part, Bonaminio is taking nothing for granted. "Nobody's doing what I'm doing, and I don't know if I'm going to be able to do it," Bonaminio says. "Ask me in a year." Whatever happens, America's most independent grocer no doubt will continue to do his own thing—and have fun doing it.

Questions

1. Which of the Big Five personality traits is Jim Bonaminio likely to be high on?
2. How would you characterize Bonaminio's values and attitudes?
3. What kinds of moods and emotions is Bonaminio likely to experience and how do these carry over into his role as founder and proprietor of Jungle Jim's International Market?
4. As the founder of Jungle Jim's, how have Bonaminio's values given rise to Jungle Jim's culture?

Source: Anthony Bianco, "The Wizard of Odd," Reprinted from the April 18, 2005, issue of *BusinessWeek* by special permission. Copyright © by McGraw-Hill Companies, Inc., pp. 82–83.

The Immelt Revolution

He's turning GE's culture upside down, demanding far more risk and innovation

Despite his air of easygoing confidence, Jeffrey R. Immelt admits to two fears: that General Electric Co. will become boring, and that his top people might act like cowards. That's right: cowards. He worries that GE's famous obsession with bottom-line results—and tendency to get rid of those who don't meet them—will make some execs shy away from taking risks that could revolutionize the company.

Immelt, 49, is clearly pushing for a cultural revolution. For the past three and one-half years, the GE chairman and CEO has been on a mission to transform the hard-driving, process-oriented company into one steeped in creativity and wired for growth. He wants to move GE's average organic growth rate—the increase in revenue that comes from existing operations, rather than deals and currency fluctuations—to at least 8 percent from about 5 percent over the past decade. Under his former boss, the renowned Jack Welch, the skills GE prized above all others were cost-cutting, efficiency, and dealmaking. What mattered was the continual improvement of operations, and that mindset helped make the \$152 billion industrial and finance behemoth a marvel of earnings consistency. Immelt hasn't turned his back on the old ways. But in his GE, the new imperatives are risk-taking, sophisticated marketing, and above all, innovation.

This is change borne of necessity. The Welch era reached its

zenith in the booming, anything-goes economy of the late 1990s. Back then, GE always seemed to beat the consensus forecasts by a penny a share—and investors felt no burning need to figure out exactly how they did it. Immelt has no such luxury. With a slower-growing domestic economy, less tolerance among investors for buying your way to growth, and more global competitors, Immelt, like many of his peers, has been forced to shift the emphasis from deals and cost-cutting to new products, services, and markets. Any other course risks a slow descent into irrelevance. "It's a different era," says Immelt, a natural salesman who still happily recounts the days when he drove around his territory in a Ford Taurus while at GE Plastics.

So how, exactly, do you make a culture as ingrained as GE's sizzle with bold thinking and creative energy? To start, you banish some long-cherished traditions and beliefs. Immelt has welcomed outsiders into the highest ranks, even making one, Sir William M. Castell, a vice-chairman. That's a serious break with GE's promote-from-within past. He is pushing hard for a more global workforce that reflects the communities in which GE operates. Immelt is also encouraging his homegrown managers to become experts in their industries rather than just experts in managing. Instead of relying on execs who barely had time to position a family photo on their desk before moving on to the next executive assign-

ment, he's diversifying the top ranks and urging his lieutenants to stay put and make a difference where they are.

Most of all, Immelt has made the need to generate blockbuster ideas more than an abstract concept. In true GE fashion, he has engineered a quantifiable and scalable process for coming up with money-making "eureka!" moments. While Welch was best known for the annual Session C meetings during which he personally evaluated the performance of GE's top several hundred managers, Immelt's highest-profile new gathering is the Commercial Council. Immelt leads the group of roughly a dozen top sales and marketing executives, including some unit heads such as GE Consumer Finance CEO David R. Nissen. The members hold phone meetings every month and meet each quarter to discuss growth strategies, think up ways to reach customers, and evaluate ideas from the senior ranks that aim to take GE out on a limb. "Jeff has launched us on a journey to become one of the best sales and marketing companies in the world," says Nissen, who describes the meetings as collegial and more experimental than other GE gatherings.

To inspire the fresh thinking he's looking for, Immelt is wielding the one thing that speaks loud and clear: money. The GE chief is tying executives' compensation to their ability to come up with ideas, show improved customer service, generate cash growth, and boost sales

instead of simply meeting bottom-line targets. As Immelt puts it, "you're not going to stick around this place and not take bets." More concretely, 20 percent of 2005 bonuses will come from meeting pre-established measures of how well a business is improving its ability to meet customer needs. And while he hasn't exactly repudiated Welch's insistence that managers cull the bottom 10 percent of their staff, insiders say there's more flexibility, more subjectivity to the process. Risking failure is a badge of honor at GE these days.

Now Immelt's main objective is to get more immediate growth out of the businesses he already has. That's where the Imagination Breakthroughs come in. Over the past 18 months, Immelt has agreed to invest \$5 billion in 80 projects that range from creating microjet engines to overhauling the brand image of 3,000 consumer-finance locations. The hope is that the first lot will generate \$25 billion in revenue by 2007—cheap, if it works, when you consider what it would cost to acquire something from the outside with that level of sales. In the next year or two, Immelt expects to have 200 such projects under way.

The pressure to produce could not be more intense. Many of the company's 307,000 workers weren't exactly hired to be part of a diverse, creative, fleet-footed army of visionaries who are acutely sensitive to customers' needs. "These guys just aren't dreamer types," says one consultant who has worked with the company. "It almost seems painful to them, like a waste of time." Even insiders who are openly euphoric about the changes under Chairman Jeff admit to feeling some fear in the depth of their guts.

To Immelt, the best managers are great marketers and not just

great operators. That's a rethinking of GE's long-held bias that winning products essentially sell themselves. Beth Comstock, who was appointed chief marketing officer three years ago with the mission of boosting the company's marketing expertise, says that when she started, a number of insiders were skittish about the new agenda: "Everyone thought, 'I've got to get into sales and marketing to be relevant in this company?'"

Well, yes. Comstock is trying to elevate the role of marketing throughout GE. She has helped develop a commercial leadership program that sends the best and brightest marketers around the organization for two intensive years, much as GE's corporate audit staff has long done on the finance side. The auditors were important to maintaining financial discipline under Welch. Now, GE has initiated new courses in marketing, as well as ones on how to spark idea generation. Some executives have also taken to holding "idea jams," where people from diverse business brainstorm. Within GE Energy alone, there are "growth heroes," who are held up as emblematic of where the company wants to go, a "virtual idea box" to spur brainstorming via the Web, and "Excellerator awards" for the development of ideas. The jargon may smack of classic GE, but the approach is novel. "This is about unlocking the curiosity, yet having the rigor stay intact," says Comstock.

Outsiders' Influence

But there's a limit to how much Immelt can transform his own people. A key strategy—and one that amounts to a gut punch to the culture—involves bringing in more outsiders. In sales and marketing alone, GE has hired more than

1,700 new faces in the past few years, including hundreds of seasoned veterans such as David J. Slump, a former ABB Group executive who is the chief marketing officer of GE Energy, "I just didn't think outsiders would do well here," says Slump, who was surprised at the unit's openness to changing its ways, though one of the senior executives did warn him about coming off as "too intense."

Immelt is also looking for more leaders who are intensely passionate about their businesses and are experts in the details. "I want to see our people become part of their industries," he says. No one represents Immelt's vision of what a GE leader should be better than Bill Castell—who has spent his entire career in one industry and who has rarely, if ever, focused on maximizing profits.

Castell is quite unlike the archetypal GE executive. He's totally immersed in his industry, a leading thinker on the future of personalized medicine who will never head up a business based on jet engines or commercial finance. Nor is he pursuing a black belt in Six Sigma or losing sleep over making his numbers. "People were surprised at first that I didn't tend to talk about the quarter," admits Castell. Yet Immelt loves him. "I want managers to have the kind of curiosity that Bill has, his passion for the industry," he says. "He understands where the market is going." This is, after all, a man known to call up his boss and wax on about an angiogenesis marker that won't hit the marketplace for 10 years. Imagine how long that conversation would have lasted with Welch.

Investors are still waiting to see whether GE's evangelizing chairman can truly make his company grow faster than the world around it. Even some of his fans think that

GE's new momentum has more to do with the overall economy than with idea generation. Says Steve Roukis of Matrix Asset Advisors, which owns 2 million GE shares: "If you have a revolutionary decade of growth around the world, who's going to be there to capture it? GE."

Capture it? Jeff Immelt wants to shape it, drive it, make it his own. For him, reinventing GE is the only way to make his company dominate

this century, much as it led the one before.

Questions

1. How would you characterize Jeffrey Immelt's personality?
2. What terminal and instrumental values are likely to be important to him?
3. What kinds of attitudes is he trying to promote within GE?

4. As he seeks to transform GE's culture, what values and norms is he emphasizing? Why?

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CHAPTER

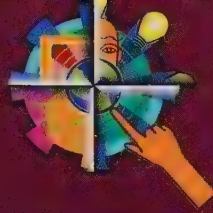
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Managing Ethics and Diversity

Learning Objectives

After studying this chapter, you should be able to:

- Illustrate how ethics help managers determine the right or proper way to behave when dealing with different stakeholder groups.
- Explain why managers should strive to create ethical organizational cultures.
- Appreciate the increasing diversity of the workforce and of the organization environment.
- Grasp the central role that managers play in the effective management of diversity.
- Understand why the effective management of diversity is both an ethical and a business imperative.
- Understand the two major forms of sexual harassment and how they can be eliminated.



Management Snapshot

How to Strengthen an Organization's Code of Ethics

How can organizations make sure their employees behave ethically?

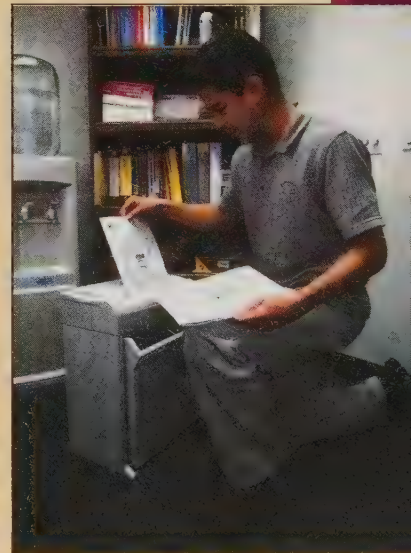
In 2002, accounting giant Arthur Andersen was found guilty of obstruction of justice for shredding documents related to its audits of Enron Corporation. Apparently, Andersen's senior partners, in their efforts to hide evidence of Andersen's fraudulent auditing of Enron's illegal accounting practices, told middle managers to shred thousands of pages of accounting documents. Andersen's illegal actions became public in 2001. But by then the company had lost the trust of most of its major clients. Merck, Freddie Mac, and Delta Airlines already had terminated their contracts with the company.

After the obstruction of justice conviction, Andersen lost its auditing license to practice accounting in the United States and the company collapsed. Andersen's partners and employees alike found themselves without jobs; they also lost much of the personal capital they had invested in the company. Andersen's managers' and employees' unethical and illegal behavior destroyed the company.

The behavior of Arthur Andersen's managers seemed out of character to many people. The company had a widely publicized, well-developed internal code of ethics that was supposed to rein in and prevent unethical and illegal behavior. When confronted with a crisis, however, Andersen's code of ethics was not followed. One reason appears to be that managers were just "going through the motions" in using the company's ethical code to make decisions. When

confronted with ethical decisions, managers failed to behave ethically in the face of their desire to promote their own self-interest.

Because of ethics scandals at many large companies in the 2000s, there has been a renewed call for companies to put "teeth" in



Usually a routine business practice, sometimes document shredding may be considered unethical or even illegal.

their ethical codes.¹ There are three main reasons for this renewed call. First, the passage of the Sarbanes-Oxley Act requires companies to do a more thorough job of policing their internal accounting practices to ensure employees accurately report sales and expenditures.² Second, the increasing number of diversity lawsuits being brought against companies by minority groups and women and costing tens of millions of dollars to settle, makes it imperative that organizations issue clear ethical guidelines about how different kinds of people and groups should be treated. Third, the increasing globalization of business focuses attention on the ethics of outsourcing jobs to countries overseas, resulting in massive job losses at home. Also workers abroad, including teenagers and children, perform jobs for very minimal wages in sweatshop conditions.

Today, many companies such as accounting firms Deloitte & Touché and PriceWaterhouseCoopers have rewritten their codes of ethics to make them more detailed and specific.³ The Sarbanes-Oxley Act requires that not only do CEOs sign and cer-

tify the accuracy of their companies' financial results so that these same CEOs can be held legally liable for the results, but also that all employees read and sign ethics statements as a condition of employment. In addition, companies are providing their managers and employees with much more detailed ethics training to instruct them on how to make ethical decisions even when the decisions might harm their own interests or the company's interests. Companies are also stepping up diversity training to ensure that employees are treated fairly and that all benefit from the real advantages of a diverse workforce.

Many kinds of software are being developed to provide ongoing surveillance and to red flag unethical behavior—such as software that can analyze reports to reveal if purchasing managers are taking “kickbacks,” or software that recognizes the transmission of offensive materials through an organization's email system and intranet. Given that many companies and CEOs have had their unethical and illegal behavior revealed through emails, the use of software to strengthen ethics codes is only likely to increase in the future.⁴

Overview

While a strong code of ethics can influence the way employees behave, what causes people to behave unethically in the first place? Moreover, how do managers and employees determine what is ethical or unethical? In this chapter, we examine the nature of the obligations and responsibilities of managers and the companies they work for toward the people and society that are affected by their actions. First, we examine the nature of ethics and the sources of ethical problems. Second, we discuss the major groups of people, called *stakeholders*, who are affected by the way companies operate. Third, we look at four rules or guidelines that managers can use to decide whether a specific business decision is ethical or unethical and why it is important for people and companies to behave in an ethical way.

We then turn to the issue of the effective management of diversity. This first requires that organizations, their managers, and all employees behave ethically and follow legal rules and regulations in the ways diverse employees are hired, promoted, and treated. Second, effectively managing diversity means learning to appreciate and respond appropriately to the needs, attitudes, beliefs, and values that diverse employees bring to an organization and finding ways to utilize their skills and talents to benefit them and the company they work for. Finally, we discuss steps managers can take to eradicate sexual harassment in organizations. By the end of this chapter you will understand the central role that the effective management of ethics and diversity plays in shaping the practice of business and the life of a people, society, and nation.

The Nature of Ethics

Suppose you see a person being mugged in the street. How will you behave? Will you act in some way to help, even though you risk being hurt? Will you walk away? Perhaps you might adopt a “middle way” and not intervene but call the police? Does the way you act depend on whether the person being mugged is a fit male, an elderly person, or even a street person? Does it depend on whether there are other people around, so you can tell yourself, “Oh well, someone else will help or call the police, I don’t need to”?

Ethical dilemmas

ethical dilemma

The quandary people find themselves in when they have to decide if they should act in a way that might help another person or group even though doing so might go against their own self-interest.

ethics The inner-guiding moral principles, values, and beliefs that people use to analyze or interpret a situation and then decide what is the “right” or appropriate way to behave.

The situation described above is an example of an **ethical dilemma**, the quandary people find themselves in when they have to decide if they should act in a way that might help another person or group, and is the “right” thing to do, even though doing so might go against their own self-interest.⁵ A dilemma may also arise when a person has to decide between two different courses of action, knowing that whichever course he or she chooses will result in harm to one person or group even while it may benefit another. The ethical dilemma here is to decide which course of action is the “lesser of two evils.”

People often know they are confronting an ethical dilemma when their moral scruples come into play and cause them to hesitate, debate, and reflect upon the “rightness” or “goodness” of a course of action. Moral scruples are thoughts and feelings that tell a person what is right or wrong; they are a part of a person’s ethics. **Ethics** are the inner-guiding moral principles, values, and beliefs that people use to analyze or interpret a situation and then decide what is the “right” or appropriate way to behave. At the same time, ethics also indicate what is inappropriate behavior and how a person should behave to avoid doing harm to another person.

The essential problem in dealing with ethical issues, and thus solving moral dilemmas, is that there are no absolute or indisputable rules or principles that can be developed to decide if an action is ethical or unethical. Put simply, different people or groups may dispute which actions are ethical or unethical depending on their own personal self-interest and specific attitudes, beliefs, and values—concepts we discussed in Chapter 2. How, therefore, are we and companies and their managers and employees to decide what is ethical and so act appropriately toward other people and groups?

Ethics and the law

The first answer to this question is that society as a whole, using the political and legal process, can lobby for and pass laws that specify what people can and cannot do. Many different kinds of laws exist to govern business, for example, laws against fraud and deception and laws governing how companies can treat their employees and customers. Laws also specify what sanctions or punishments will follow if those laws are broken. Different groups in society lobby for which laws should be passed based on their own personal interests and beliefs with regard to what is right or wrong. The group that can summon most support is able to pass the laws that most closely align with its interests and beliefs. Once a law is passed, a decision about what the appropriate behavior is with regard to a person or situation is taken from the personally determined ethical realm to the societally determined legal realm. If

you do not conform to the law, you can be prosecuted; and if you are found guilty of breaking the law, you can be punished. You have little say in the matter; your fate is in the hands of the court and its lawyers.

In studying the relationship between ethics and law, it is important to understand that *neither laws nor ethics are fixed principles*, cast in stone, that do not change over time. Ethical beliefs alter and change as time passes, and as they do so, laws change to reflect the changing ethical beliefs of a society. It was seen as ethical, and it was legal, for example, to acquire and possess slaves in ancient Rome and Greece and in the United States until the 19th century. Ethical views regarding whether slavery was morally right or appropriate changed, however. Slavery was made illegal in the United States when those in power decided that slavery degraded the very meaning of being human. Slavery is a statement about the value or worth of human beings and about their right to life, liberty, and the pursuit of happiness. And if I deny these rights to other people, how then can I claim to have any natural or “god-given” rights to these things myself?

Moreover, what is to stop any person or group that becomes powerful enough to take control of the political and legal process from enslaving me and denying me the right to be free and to own property? In denying freedom to others, one risks losing it oneself, just as stealing from others opens the door for them to steal from me in return. “Do unto others as you would have them do unto you” is a commonly used ethical or moral rule that people apply in such situations to decide what is the right thing to do. This moral rule is discussed in detail below.

Changes in ethics over time

There are many types of behavior—such as murder, theft, slavery, rape, driving while intoxicated—that most, if not all, people currently believe are totally unacceptable and unethical and should therefore be illegal. There are also, however, many other kinds of actions and behaviors whose ethical nature is open to dispute. Some people might believe that a particular behavior—for example, smoking tobacco or possessing guns—is unethical and so should be made illegal. Others might argue that it is up to the individual or a group to decide if such behaviors are ethical or not and thus whether a particular behavior should remain legal.

As ethical beliefs change over time, some people may begin to question whether existing laws that make specific behaviors illegal are still appropriate today. They might argue that although a specific behavior is deemed illegal, this does not make it unethical and thus the law should be changed. In the United States, for example, it is illegal to possess or use marijuana (cannabis). To justify this law, it is commonly argued that smoking marijuana leads people to try more dangerous drugs. Once the habit of taking drugs has been acquired, people can get hooked on them. More powerful drugs such as the murderous heroin are fearfully addictive, and most people cannot stop using them without help from others. Thus, the use of marijuana, because it might lead to further harm, is an unethical practice.

It has been documented medically, however, that the use of marijuana has many medical benefits for people with certain illnesses. For example, for cancer sufferers who are undergoing chemotherapy and for those with AIDS who are on potent medications, marijuana offers relief from many of the treatment’s side effects, such as nausea and lack of appetite. Yet, in the United States, it is illegal in many states for doctors to prescribe marijuana for these patients, so their suffering goes on. Since 1996, however, 35 states have made it legal to prescribe marijuana for

medical purposes; nevertheless, the federal government has sought to stop such state legislation. People in many states are currently lobbying for a relaxation of the law against the use of marijuana for medical purposes, and in June 2004 the U.S. Supreme Court agreed to hear the case on the medical use of the drug.⁶ In Canada there has been a widespread movement to decriminalize marijuana. While not making the drug legal, decriminalization removes the threat of prosecution even for uses that are not medically related. A major ethical debate is currently raging over this issue in many countries.

The important point to note is that while ethical beliefs lead to the development of laws and regulations to prevent certain behaviors or encourage others, laws themselves can and do change or even disappear as ethical beliefs change. In Britain in 1830 there were over 350 different crimes for which a person could be executed, including sheep stealing. Today there are none; capital punishment and the death penalty are no longer legal. Thus, both ethical and legal rules are relative: No absolute or unvarying standards exist to determine how we should behave, and people are caught up in moral dilemmas all the time. Because of this we have to make ethical choices.

The discussion above highlights an important issue in understanding the relationship between ethics, law, and business. In the early 2000s, many scandals plagued major companies such as Enron, Arthur Andersen, WorldCom, Tyco, and others. Managers in some of these companies clearly broke the law and used illegal means to defraud investors. At Enron, former chief financial officer Andrew Fastow, and his wife, pleaded guilty to falsifying the company's books so that they could siphon off tens of millions of dollars of Enron's money for their own use.



Coldbath Fields Prison, London, circa 1810. The British criminal justice system around this time was quite severe: There were over 350 different crimes for which a person could be executed, including sheep stealing. Thankfully in this case, as ethical beliefs change over time, so do laws.

In other cases, some managers took advantage of loopholes in the law to divert hundreds of millions of dollars of company capital into their own personal fortunes. At WorldCom, for example, former CEO Bernie Ebbers used his position to place six personal, long-time friends on its 13-member board of directors. While this is not illegal, obviously these people would vote in his favor at board meetings. As a result of their support Ebbers received huge stock options and a personal loan of over \$150 million from WorldCom. In return, his supporters were well rewarded for being directors; for example, Ebbers allowed them to use WorldCom's corporate jets for a minimal cost—something that saved them hundreds of thousands of dollars a year.⁷

In the light of these events some people said, “Well, what these people did was not illegal,” implying that because such behavior was not illegal it was also not unethical. However, not being illegal does *not* make it ethical; such behavior is clearly unethical.⁸ In many cases laws are passed *later* to close the loopholes and prevent unethical people, such as Fastow and Ebbers, from taking advantage of them to pursue their own self-interest at the expense of others. Like ordinary people, managers must confront the need to decide what is appropriate and inappropriate as they use a company's resources to produce goods and services for customers⁹ and decide how to balance their own self-interest against the self-interest of other stakeholders.

Stakeholders and Ethics

Just as people have to work out the right and wrong ways to act, so do companies. When the law does not specify how companies should behave, their managers must decide what is the right or ethical way to behave toward the

people and groups affected by their actions. Who are the people or groups that are affected by a company's business decisions? If a company behaves in an ethical way, how does this benefit people and society? Conversely, how are people harmed by a company's unethical actions?

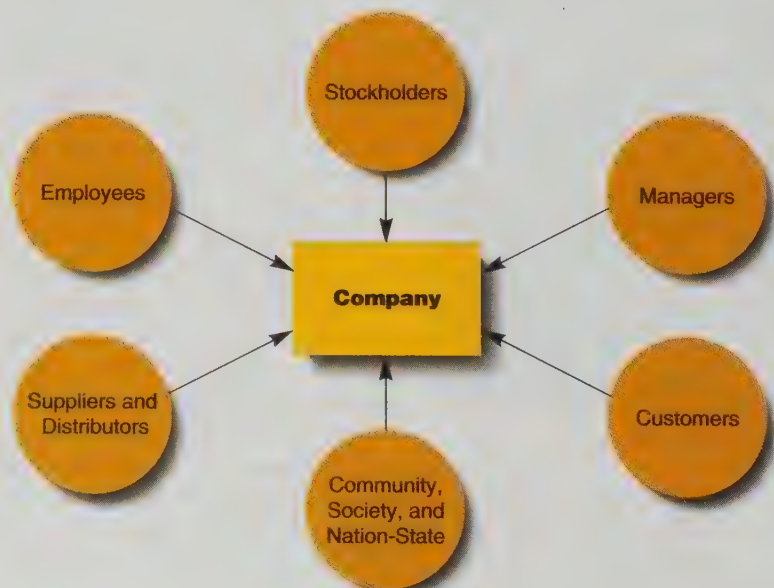
stakeholders The people and groups that supply a company with its productive resources and so have a claim on and stake in the company.

The people and groups affected by the way a company and its managers behave are called its stakeholders. **Stakeholders** supply a company with its productive resources; as a result, they have a claim on and stake in the company.¹⁰ Since stakeholders can directly benefit or be harmed by its actions, the ethics of a company and its managers are important to them. Who are a company's major stakeholders? What do they contribute to a company, and what do they claim in return? Below we examine the claims of these stakeholders—stockholders, managers, employees, suppliers and distributors, customers, and community, society, and nation-state (Figure 3.1).

Stockholders

Stockholders have a claim on a company because when they buy its stock or shares they become its owners. Whenever the founder of a company decides to publicly incorporate the business to raise capital, shares of the stock of that company are issued. This stock grants its buyers ownership of a certain percentage of the company and the right to receive any future stock dividends. For example, in 2003, Microsoft had over \$46 billion in cash, money it retained in the company to fund its future operations. After pressure from shareholders it declared a dividend of 31 cents per share for the owners of its 5 billion shares; Bill Gates received \$100 million in dividends based on his stockholding.

Figure 3.1
Types of
Company
Stakeholders



Stockholders are interested in the way a company operates because they want to maximize the return on their investment. Thus, they watch the company and its managers closely to ensure that management is working diligently to increase the company's profitability.¹¹ Stockholders also want to ensure that managers are behaving ethically and not risking investors' capital by engaging in actions that could hurt the company's reputation. The fall of Enron from being one of the biggest and most profitable companies in the United States to declaring bankruptcy took less than one year after the illegal and unethical actions of its top managers came to light. The Enron tragedy was brought about by a handful of greedy top managers who abused their positions of trust. It has been estimated that Enron's collapse, by precipitating the crash of the stock market, caused the average U.S. household to lose over \$66,000 of its hard-earned savings as trillions of dollars were wiped off the value of the stock of publicly traded U.S. companies.

Managers

Managers are a vital stakeholder group because they are responsible for using a company's financial capital and human resources to increase its performance and thus its stock price.¹² Managers have a claim on an organization because they bring to it their skills, expertise, and experience. They have the right to expect a good return or reward by investing their human capital to improve a company's performance. Such rewards include good salaries and benefits, the prospect of promotion and a career, and stock options and bonuses tied to company performance.

Managers are the stakeholder group with the responsibility of deciding which goals an organization should pursue to most benefit stakeholders and how to make the most efficient use of resources to achieve those goals. In making such decisions, managers are frequently in the position of having to juggle the interests of different stakeholders, including themselves.¹³ These decisions are sometimes very difficult and challenge managers to uphold ethical values because in some cases decisions that benefit some stakeholder groups (managers and stockholders) harm other groups (individual workers and local communities). For example, in economic downturns or when a company experiences performance shortfalls, layoffs may help to cut costs (thus benefiting shareholders) at the expense of the employees laid off. Many U.S. managers have recently been faced with this very difficult decision—over 700,000 layoffs were announced in the first six months of 2001 according to Challenger, Gray, and Christmas (a firm specializing in outplacement services).¹⁴ Layoff decisions are always difficult, as they not only take a heavy toll on workers, their families, and local communities but also mean the loss of the contributions of valued employees to an organization. Whenever decisions such as these are made—benefiting some groups at the expense of others—ethics come into play.

As we discussed in Chapter 1, managers must be motivated and given incentives to work hard in the interests of stockholders. Their behavior must also be scrutinized to ensure they do not behave illegally or unethically, pursuing goals that threaten stockholders and the company's interests.¹⁵ Unfortunately, we have seen in the 2000s how easy it is for top managers to find ways to ruthlessly pursue their self-interest at the expense of stockholders and employees because laws and regulations were not strong enough to force them to behave ethically.

In a nutshell, the problem has been that in many companies corrupt managers focus not on building the company's capital and stockholders' wealth but on

maximizing their own *personal capital and wealth*. In an effort to prevent future scandals the Securities and Exchange Commission (SEC), the government's top business watchdog, began in 2003 to rework the rules governing a company's relationship with its auditor, as well as regulations concerning stock options, and to increase the power of outside directors to scrutinize a CEO. The SEC's goal is to turn many acts that were only unethical behavior in 2003 into illegal behavior in the near future. Managers could then be prosecuted if they engage in these acts.

Many experts are also arguing that the rewards given to top managers, particularly the CEO and COO, have grown out of control since the 1990s. Top managers are the new "aristocrats" today; through their ability to influence the board of directors and raise their own pay, they have amassed personal fortunes worth hundreds of millions of dollars. For example, while in 1982 a typical CEO earned about 18 times as much as the average worker, by 2002 that number had risen to 2,600 times as much—a staggering increase. Michael Eisner, CEO of Disney, has received over \$800 million in Disney stock options. Jack Welch, the former CEO of General Electric and one of the most admired managers in the United States, received more than \$500 million in GE stock options as a reward for his services. On his retirement he was also awarded \$2.5 million in annual perks ranging from round-the-clock access to a corporate jet to free dry cleaning. When this information was revealed to the press, Welch quickly agreed to pay GE \$2 million for these services.

Is it ethical for top managers to receive such vast amounts of money from their companies? Do they really earn it? Remember, this money could have gone to shareholders in the form of dividends. It could also have gone to reduce the huge salary gap between those at the top and those at the bottom of the hierarchy. Many people argue that the growing disparity between the rewards given to CEOs and to other employees is unethical and should be regulated. CEO pay has become too high because CEOs are the people who set and control one another's salaries and bonuses! They can do this because they sit on the boards of other companies, as outside directors, and thus can control the salaries and stock options paid to other CEOs. As the example of Bernie Ebbers at WorldCom, discussed earlier, suggests, when a CEO can control and select many of the outside directors, the CEO can abuse his or her power.

Others argue that because top managers play an important role in building a company's capital and wealth, they deserve a significant share of its profits. Jack Welch, for example, deserved his \$500 million because he created hundreds of billions of dollars in stockholder wealth. The debate over how much money CEOs and other top managers should be paid is currently raging.

Employees

A company's employees are the hundreds of thousands of people who work in its various departments and functions, such as research, sales, and manufacturing. Employees expect that they will receive rewards consistent with their performance. One principal way that a company can act ethically toward employees and meet their expectations is by creating an occupational structure that fairly and equitably rewards employees for their contributions. Companies, for example, need to develop recruitment, training, performance appraisal, and reward systems that do not discriminate between employees and that employees believe are fair.

Suppliers and distributors

No company operates alone. Every company is in a network of relationships with other companies that supply it with the inputs (e.g., raw materials, component parts, contract labor, and clients) that it needs to operate. It also depends on intermediaries such as wholesalers and retailers to distribute its products to the final customer. Suppliers expect to be paid fairly and promptly for their inputs; distributors expect to receive quality products at agreed-upon prices.

Once again, many ethical issues arise in the way companies contract and interact with their suppliers and distributors. Important issues concerning how and when payments are to be made or product quality specifications are governed by the terms of the legal contracts a company signs with its suppliers and distributors. Many other issues are dependent on business ethics. For example, numerous products sold in U.S. stores have been outsourced to countries that do not have U.S.-style regulations and laws to protect the workers who make these products. All companies must take an ethical position on the way they obtain and make the products they sell. Commonly this stance is published on the company's Web site. Table 3.1 presents part of the The Gap's statement on its approach to global ethics (www.thegap.com).

Customers

Customers are often regarded as the most critical stakeholder group since if a company cannot attract them to buy its products, it cannot stay in business. Thus, managers and employees must work to increase efficiency and effectiveness in order to create loyal customers and attract new ones. They do so by selling customers quality products at a fair price and providing good after-sales service. They can also strive to improve their products over time.

Many laws exist that protect customers from companies that attempt to provide dangerous or shoddy products. Laws exist that allow customers to sue a company whose product causes them injury or harm, such as a defective tire or vehicle. Other laws force companies to clearly disclose the interest rates they charge on purchases—an important hidden cost that customers frequently do not factor into their purchase decisions. Every year thousands of companies are prosecuted for breaking these laws, so “buyer beware” is an important rule customers must follow when buying goods and services.

Community, society, and nation

The effects of the decisions made by companies and their managers permeate all aspects of the communities, societies, and nations in which they operate. *Community* refers to physical locations like towns or cities or to social milieus like ethnic neighborhoods in which companies are located. A community provides a company with the physical and social infrastructure that allows it to operate; its utilities and labor force; the homes in which its managers and employees live; the schools, colleges, and hospitals that service their needs; and so on.

Through the salaries, wages, and taxes it pays, a company contributes to the economy of the town or region and often determines whether the community prospers or declines. Similarly, a company affects the prosperity of a society and a nation and, to the degree that a company is involved in global trade, all the countries

Table 3.1**Some Principles from the Gap's Code of Vendor Conduct**

As a condition of doing business with Gap Inc., each and every factory must comply with this Code of Vendor Conduct. Gap Inc. will continue to develop monitoring systems to assess and ensure compliance. If Gap Inc. determines that any factory has violated this Code, Gap Inc. may either terminate its business relationship or require the factory to implement a corrective action plan. If corrective action is advised but not taken, Gap Inc. will suspend placement of future orders and may terminate current production.

I. General Principles

Factories that produce goods for Gap Inc. shall operate in full compliance with the laws of their respective countries and with all other applicable laws, rules and regulations.

II. Environment

Factories must comply with all applicable environmental laws and regulations. Where such requirements are less stringent than Gap Inc.'s own, factories are encouraged to meet the standards outlined in Gap Inc.'s statement of environmental principles.

III. Discrimination

Factories shall employ workers on the basis of their ability to do the job, without regard to race, color, gender, nationality, religion, age, maternity or marital status.

IV. Forced Labor

Factories shall not use any prison, indentured or forced labor.

V. Child Labor

Factories shall employ only workers who meet the applicable minimum legal age requirement or are at least 14 years of age, whichever is greater. Factories must also comply with all other applicable child labor laws. Factories are encouraged to develop lawful workplace apprenticeship programs for the educational benefit of their workers, provided that all participants meet both Gap Inc.'s minimum age standard of 14 and the minimum legal age requirement.

VI. Wages & Hours

Factories shall set working hours, wages and overtime pay in compliance with all applicable laws. Workers shall be paid at least the minimum legal wage or a wage that meets local industry standards, whichever is greater. While it is understood that overtime is often required in garment production, factories shall carry out operations in ways that limit overtime to a level that ensures humane and productive working conditions.

it operates in and thus the prosperity of the global economy. We have already discussed the many issues surrounding global outsourcing and the loss of jobs in the United States, for example.

Although the individual effects of the way each McDonald's restaurant operates might be small, for instance, the combined effects of the way all McDonald's and other fast-food companies do business are enormous. In the United States alone, over 500,000 people work in the fast-food industry, and many thousands of suppliers like farmers, paper cup manufacturers, builders, and so on, depend on it for their livelihood. Small wonder then that the ethics of the fast-food business are scrutinized closely. The industry is the major lobbyist against attempts to raise the national minimum wage, which was \$5.15 in 2004, because a higher minimum wage would substantially increase its operating costs. However, responding to protests about chickens raised in cages where they cannot move their wings, McDonald's—the largest egg buyer in the United States—issued new ethical guidelines concerning cage size and related matters that its egg suppliers must abide by if they are to retain



In 2001 McDonald's announced new standards that would require egg suppliers to improve the conditions under which chickens are housed and treated. Since McDonald's is an important customer, suppliers are likely to follow these new standards.

its business. What ethical rules does McDonald's use to decide its stance toward minimum pay or minimum cage size?

Business ethics are also important because the failure of companies can have catastrophic effects on a community; a general decline in business activity affects a whole nation. The decision of a large company to pull out of a community, for example, can seriously threaten the community's future. Some companies may attempt to improve their profits by engaging in actions that, although not illegal, can hurt communities and nations. One of these actions is pollution. Many U.S. companies reduce costs by trucking their waste to Mexico, where it is legal to dump waste in the Rio Grande. The dumping pollutes the river from the Mexican side, and the effects are increasingly being felt on the U.S. side too.

Rules for ethical decision making

When a stakeholder perspective is taken, questions on company ethics abound.¹⁶ What is the appropriate way to manage the claims of all stakeholders? Company decisions that favor one group of stakeholders, for example, are likely to harm the interests of others.¹⁷ High prices to customers may lead to high returns to shareholders and high salaries for managers in the short run. If in the long run customers turn to companies that offer lower-cost products, however, the result may be declining sales, laid-off employees, and the decline of the communities that support the high-price company's business activity.

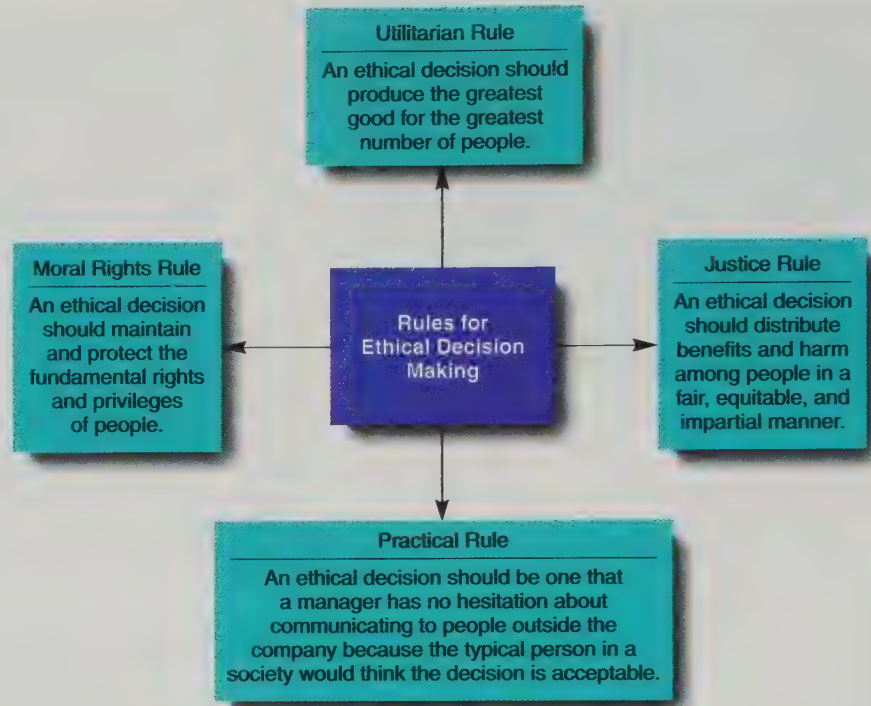
When companies act ethically, their stakeholders support them. For example, when banks are willing to supply them with new capital, companies attract highly qualified job applicants, and new customers are drawn to their products. Thus ethical companies grow and expand over time, and all their stakeholders benefit. The result of unethical behavior is the loss of reputation and resources, shareholders who sell their shares, skilled managers and employees who leave the company, and customers who turn to the products of more reputable companies.

When making business decisions, managers must take the claims of all stakeholders into consideration.¹⁸ To help themselves and employees make ethical decisions and behave in ways that benefit their stakeholders, managers can use four ethical rules or principles to analyze the effects of their business decisions on stakeholders: the *utilitarian*, *moral rights*, *justice*, and *practical* rules (Figure 3.2).¹⁹ These rules are useful guidelines that help managers decide on the appropriate way to behave in situations where it is necessary to balance a company's self-interest against the interests of its stakeholders. Remember, the right choices will lead resources to be used where they can create the most value. If all companies make the right choices, all stakeholders will benefit in the long run.²⁰

utilitarian rule An ethical decision is a decision that produces the greatest good for the greatest number of people.

UTILITARIAN RULE The **utilitarian rule** is that an ethical decision is a decision that produces the greatest good for the greatest number of people. To decide which is the most ethical course of business action, managers should first consider

Figure 3.2
Four Ethical
Rules



how different possible courses of business action would benefit or harm different stakeholders. They should then choose the course of action that provides the most benefits, or conversely the one that does the least harm, to stakeholders.²¹

The ethical dilemma for managers is, How do you measure the benefits and harms that will be done to each stakeholder group? Moreover, how do you evaluate the rights of different stakeholder groups, and the relative importance of each group, in coming to a decision? Since stockholders are the owners of the company, shouldn't their claims be held above those of employees? For example, managers might be faced with a choice of using global outsourcing to reduce costs and lower prices to customers or continuing with high-cost production at home. A decision to use global outsourcing benefits shareholders and customers but will result in major layoffs that will harm employees and the communities in which they live. Typically, in a capitalist society, like the United States, the interests of shareholders are put above those of employees, so production will move abroad. This is commonly regarded as being an ethical choice because in the long run the alternative, home production, might cause the business to collapse and go bankrupt, in which case greater harm will be done to all stakeholders.

moral rights rule

An ethical decision is one that best maintains and protects the fundamental or inalienable rights and privileges of the people affected by it.

MORAL RIGHTS RULE Under the **moral rights rule**, an ethical decision is a decision that best maintains and protects the fundamental or inalienable rights and privileges of the people affected by it. For example, ethical decisions protect people's rights to freedom, life and safety, property, privacy, free speech, and freedom of conscience. The adage "Do unto others as you would have them do unto you" is a moral rights principle that managers should use to decide which rights to uphold. Customers must also consider the rights of the companies and people who create the products they wish to consume.

From a moral rights perspective, managers should compare and contrast different courses of business action on the basis of how each course will affect the rights of the company's different stakeholders. Managers should then choose the course of action that best protects and upholds the rights of *all* the stakeholders. For example, decisions that might result in significant harm to the safety or health of employees or customers would clearly be unethical choices.

The ethical dilemma for managers is that decisions that will protect the rights of some stakeholders often will hurt the rights of others. How should they choose which group to protect? For example, in deciding whether it is ethical to snoop on employees, or search them when they leave work to prevent theft, does an employee's right to privacy outweigh an organization's right to protect its property? Suppose a co-worker is having personal problems and is coming in late and leaving early, placing you in the position of being forced to pick up the person's workload. Do you tell your boss even though you know this will probably get that person fired?

justice rule An ethical decision is a decision that distributes benefits and harms among people and groups in a fair, equitable, or impartial way.

JUSTICE RULE The **justice rule** is that an ethical decision is a decision that distributes benefits and harms among people and groups in a fair, equitable, or impartial way. Managers should compare and contrast alternative courses of action based on the degree to which they will result in a fair or equitable distribution of outcomes for stakeholders. For example, employees who are similar in their level of skill, performance, or responsibility should receive the same kind of pay. The allocation of outcomes should not be based on differences such as gender, race, or religion.

The ethical dilemma for managers is to determine the fair rules and procedures for distributing outcomes to stakeholders. Managers must not give people they like bigger raises than they give to people they do not like or bend the rules to help their favorites. On the other hand, if employees want managers to act fairly toward them, then employees need to act fairly toward their companies and work hard and be loyal. Similarly, customers need to act fairly toward a company if they expect it to be fair to them—something people who illegally copy digital media should consider.

practical rule An ethical decision is one that a manager has no reluctance about communicating to people outside the company because the typical person in a society would think it is acceptable.

PRACTICAL RULE Each of the above rules offers a different and complementary way of determining whether a decision or behavior is ethical, and all three rules should be used to sort out the ethics of a particular course of action. Ethical issues, as we just discussed, are seldom clear-cut, however, because the rights, interests, goals, and incentives of different stakeholders often conflict. For this reason many experts on ethics add a fourth rule to determine whether a business decision is ethical: The **practical rule** is that an ethical decision is one that a manager has no hesitation or reluctance about communicating to people outside the company because the typical person in a society would think it is acceptable. A business decision is probably acceptable on ethical grounds if a manager can answer yes to each of these questions:

1. Does my decision fall within the accepted *values* or *standards* that typically apply in business activity today?
2. Am I willing to see the decision *communicated* to all people and groups *affected* by it—for example, by having it reported in newspapers or on television?
3. Would the people with whom I have a *significant* personal relationship, such as family members, friends, or even managers in other organizations, *approve* of the decision?

Applying the practical rule to analyze a business decision ensures that managers are taking into account the interests of all stakeholders.²² After applying this rule managers can judge if they have chosen to act in an ethical or unethical way and they must abide by the consequences.

Why should managers behave ethically?

Why is it so important that managers, and people in general, should act ethically and temper their pursuit of self-interest by considering the effects of their actions on others? The answer is that the relentless pursuit of self-interest can lead to a collective disaster when one or more people start to profit from being unethical because this encourages other people to act in the same way.²³ Quickly, more and more people jump onto the bandwagon, and soon everybody is trying to manipulate the situation in the way that best serves his or her personal ends with no regard for the effects of the action on others; when this happens what is often called the “tragedy of the commons” occurs.

Suppose that in an agricultural community there is common land that everybody has an equal right to use. Pursuing self-interest, each farmer acts to make the maximum use of the free resource by grazing his or her own cattle and sheep. Collectively, all the farmers overgraze the land, which quickly becomes worn out. Then a strong wind blows away the exposed topsoil, so the common land is destroyed. The pursuit of individual self-interest with no consideration for societal interests leads to disaster for each individual and for the whole society because scarce resources are destroyed.²⁴

We can look at the effects of unethical behavior on business commerce and activity in another way. Suppose companies and their managers operate in an unethical society, meaning one in which stakeholders routinely try to cheat and defraud one another. If stakeholders expect each other to cheat, how long will it take them to negotiate the purchase and shipment of products? When they do not trust each other, stakeholders will probably spend hours bargaining over fair prices, and this is a largely unproductive activity that reduces efficiency and effectiveness.²⁵ All the time and effort that could be spent improving product quality or customer service is being lost because it is spent on negotiating and bargaining. Thus, unethical behavior ruins business commerce, and society has a lower standard of living because fewer goods and services are produced, as Figure 3.3 illustrates.

On the other hand, suppose companies and their managers operate in an ethical society, meaning that stakeholders believe they are dealing with others who are basically moral and honest. In this society stakeholders have a greater reason to **trust** others, which means they have more confidence and faith in the other person's goodwill. When trust exists, stakeholders are more likely to signal their good intentions by cooperating and providing information that makes it easier to trade and price goods and services. When one party does so, this encourages others to act in the same way. Over time greater trust between stakeholders allows them to work together more efficiently and effectively, and this raises company performance (see Figure 3.3). As people see the positive results of acting in an honest way, ethical behavior becomes a valued social norm and society in general becomes increasingly ethical.

As noted in Chapter 1, one of the major tasks of managers is to protect and nurture the resources under their control. Any organizational stakeholders—managers, workers, stockholders, suppliers—who advance their own interests by behaving

trust A person's confidence and faith in another person's goodwill.

Figure 3.3
Some Effects
of Ethical and
Unethical
Behavior



unethically toward other stakeholders, either by taking resources or by denying resources to others, waste collective resources. If other individuals or groups copy the behavior of the unethical stakeholder (“If he can do it, we can do it, too”), the rate at which collective resources are misused increases, and eventually there are few resources for producing goods and services. Unethical behavior that goes unpunished creates incentives for people to put their unbridled self-interests above the rights of others.²⁶ When this happens, the benefits that people reap from joining together in organizations disappear very quickly.

An important safeguard against unethical behavior is the potential for loss of reputation.²⁷ **Reputation**, the esteem or high repute that individuals or organizations gain when they behave ethically, is an important asset. Stakeholders have valuable reputations that they must protect because their ability to earn a living and obtain resources in the long run depends on the way they behave on a day-to-day, week-to-week, and month-to-month basis.

If a manager misuses resources and other parties regard that behavior as being at odds with acceptable standards, the manager’s reputation will suffer. Behaving unethically in the short run can have serious long-term consequences. A manager who has a poor reputation will have difficulty finding employment with other companies. Stockholders who see managers behaving unethically may refuse to invest

reputation The esteem or high repute that individuals or organizations gain when they behave ethically.

in their companies, and this will decrease the stock price, undermine the companies' reputations, and ultimately put the managers' jobs at risk.²⁸

All stakeholders have reputations to lose. Suppliers who provide shoddy inputs find that organizations learn over time not to deal with them, and eventually they go out of business. Powerful customers who demand ridiculously low prices find that their suppliers become less willing to deal with them, and resources ultimately become harder for them to obtain. Workers who shirk responsibilities on the job find it hard to get new jobs when they are fired. In general, if a manager or company is known for being unethical, other stakeholders are likely to view that individual or organization with suspicion and hostility, and the reputation of each will be poor. But if a manager or company is known for ethical business practices, each will develop a good reputation.²⁹

In summary, in a complex, diverse society, stakeholders, and people in general, need to recognize they are all part of a larger social group. The way in which they make decisions and act not only affects them personally but also affects the lives of many other people. The problem is that for some people in their daily struggle to survive and succeed they totally disregard the rights of others and this can lead them to lose that "bigger" connection to other people. We can see our relationships to our families and friends, to our school, church, and so on. But, we need always to go further and keep in mind the effects of our actions on other people who will be judging our actions and whom we might harm by acting unethically. Our moral scruples are like that "other person" but are inside our heads.

Sources of an organization's code of ethics

Codes of ethics are formal standards and rules, based on beliefs about right or wrong, that managers can use to help themselves make appropriate decisions with regard to the interests of their stakeholders.³⁰ As we discuss in the opening case, today companies need to strengthen these codes and find better ways to enforce them. Ethical standards embody views about abstractions such as justice, freedom, equity, and equality. An organization's code of ethics derives from three principal sources in the organizational environment: *societal* ethics, *professional* ethics, and the *individual* ethics of the organization's managers and employees (see Figure 3.4).

societal ethics

Standards that govern how members of a society are to deal with each other on issues such as fairness, justice, poverty, and the rights of the individual.

SOCIETAL ETHICS *Societal ethics* are standards that govern how members of a society deal with each other in matters involving issues such as fairness, justice, poverty, and the rights of the individual. Societal ethics emanate from a society's laws, customs, and practices, and from the unwritten attitudes, values, and norms that influence how people interact with each other. People in a particular country may automatically behave ethically because they have internalized values and norms that specify how they should behave in certain situations. Not all values and norms are internalized, however. The typical ways of doing business in a society and laws governing the use of bribery and corruption are the result of decisions made and enforced by people with the power to determine what is appropriate.

Societal ethics vary among societies. For example, ethical standards accepted in the United States are not accepted in all other countries. In many economically poor countries bribery is standard practice to get things done, such as getting a

Figure 3.4
Sources of an
Organization's
Code of Ethics



telephone installed or a contract awarded. In the United States and many other Western countries, bribery is considered unethical and often illegal.

Societal ethics control self-interested behavior by individuals and organizations—behavior threatening to society’s collective interests. Laws spelling out what is good or appropriate business practice provide benefits to everybody. Free and fair competition among organizations is possible only when laws and rules level the playing field and define what behavior is acceptable or unacceptable in certain situations. For example, it is ethical for a manager to compete with managers in other companies by producing a higher-quality or lower-priced product, but it is not ethical (or legal) to do so by spreading false claims about competitors’ products, bribing stores to exclude competitors’ products, or blowing up competitors’ factories.

professional ethics
 Standards that govern how members of a profession are to make decisions when the way they should behave is not clear-cut.

PROFESSIONAL ETHICS Professional ethics are standards that govern how members of a profession, managers or workers, make decisions when the way in which they should behave is not clear-cut.³¹ Medical ethics govern the way doctors and nurses are to treat patients. Doctors are expected to perform only necessary medical procedures and to act in the patient’s interest and not in their own. The ethics of scientific research require scientists to conduct their experiments and present their findings in ways that ensure the validity of their conclusions. Like society at large, most professional groups can impose punishments for violations of ethical standards. Doctors and lawyers can be prevented from practicing their professions if they disregard professional ethics and put their own interests first.

Within an organization, professional rules and norms often govern how employees such as lawyers, researchers, and accountants make decisions and act in certain situations, and these rules and norms may become part of the organization’s code of ethics. When they do, workers internalize the rules and norms of their profession (just as they do those of society) and often follow them automatically when deciding

how to behave.³² Because most people follow established rules of behavior, people often take ethics for granted. However, when professional ethics are violated, such as when scientists fabricate data to disguise the harmful effects of products, ethical issues rise to the forefront of attention.

individual ethics

Personal values and attitudes that govern how individuals interact with other people.

INDIVIDUAL ETHICS **Individual ethics** are personal values (both terminal and instrumental) and attitudes that govern how individuals interact with other people.³³ Sources of individual ethics include the influence of one's family, peers, and upbringing in general, and an individual's personality and experience. The experiences gained over a lifetime—through membership in significant social institutions such as schools and religions, for example—also contribute to the development of the personal standards and values that a person applies to decide what is right or wrong and whether to perform certain actions or make certain decisions. Many decisions or behaviors that one person finds unethical, such as using animals for cosmetics testing, may be acceptable to another person because of differences in their personalities, values, and attitudes (see Chapter 2).

Ethical organizational cultures

Managers can emphasize the importance of ethical behavior and social responsibility by ensuring that ethical values and norms are a central component of organizational culture. An organization's code of ethics guides decision making when ethical questions arise, but managers can go one step farther by ensuring that important ethical values and norms are key features of an organization's culture. For example, Herb Kelleher and Southwest Airlines' culture value employee well-being; this emphasis translates into norms dictating that layoffs should be avoided.³⁴ Ethical values and norms such as these that are part of an organization's culture help organizational members resist self-interested action and recognize that they are part of something bigger than themselves.³⁵

Managers' role in developing ethical values and standards in other employees is very important. Employees naturally look to those in authority to provide leadership, and managers become ethical role models whose behavior is scrutinized by their subordinates. If top managers are not ethical, their subordinates are not likely to behave in an ethical manner. Employees may think that if it's all right for a top manager to engage in dubious behavior, it's all right for them, too. The actions of top managers such as CEOs and the president of the United States are scrutinized so closely for ethical improprieties because these actions represent the values of their organizations and, in the case of the president, the values of the nation.

Managers can also provide a visible means of support to develop an ethical culture. Increasingly, organizations are creating the role of ethics officer, or **ethics ombudsman**, to monitor their ethical practices and procedures. The ethics ombudsman is responsible for communicating ethical standards to all employees, for designing systems to monitor employees' conformity to those standards, and for teaching managers and nonmanagerial employees at all levels of the organization how to respond to ethical dilemmas appropriately.³⁶ Because the ethics ombudsman has organizationwide authority, organizational members in any department can communicate instances of unethical behavior by their managers or co-workers without fear of retribution. This arrangement makes it easier for everyone to behave ethically. In addition, ethics ombudsmen can provide guidance when organizational members are uncertain about whether an action is ethical. Some organizations

ethics ombudsman

An ethics officer who monitors an organization's practices and procedures to be sure they are ethical.

Figure 3.5**Johnson &
Johnson's Credo****Our Credo**

We believe our first responsibility is to the doctors, nurses and patients,
to mothers and fathers and all others who use our products and services.
In meeting their needs everything we do must be of high quality.

We must constantly strive to reduce our costs
in order to maintain reasonable prices.

Customers' orders must be serviced promptly and accurately.
Our suppliers and distributors must have an opportunity
to make a fair profit.

We are responsible to our employees,
the men and women who work with us throughout the world.
Everyone must be considered as an individual.

We must respect their dignity and recognize their merit.
They must have a sense of security in their jobs.

Compensation must be fair and adequate,
and working conditions clean, orderly and safe.
We must be mindful of ways to help our employees fulfill
their family responsibilities.

Employees must feel free to make suggestions and complaints.
There must be equal opportunity for employment, development
and advancement for those qualified.

We must provide competent management,
and their actions must be just and ethical.

We are responsible to the communities in which we live and work
and to the world community as well.

We must be good citizens—support good works and charities
and bear our fair share of taxes.

We must encourage civic improvements and better health and education.
We must maintain in good order
the property we are privileged to use,
protecting the environment and natural resources.

Our final responsibility is to our stockholders.

Business must make a sound profit.

We must experiment with new ideas.

Research must be carried on, innovative programs developed
and mistakes paid for.

New equipment must be purchased, new facilities provided
and new products launched.

Reserves must be created to provide for adverse times.

When we operate according to these principles,
the stock holders should realize a fair return.

Johnson + Johnson

Source: Johnson & Johnson Annual Report. Copyright © Johnson & Johnson. Used with permission.

have an organizationwide ethics committee to provide guidance on ethical issues and help write and update the company code of ethics.

Ethical organizational cultures also encourage organizational members to behave in a socially responsible manner. In fact, managers at Johnson & Johnson take social responsibility so seriously that their organization is frequently mentioned as an example of a socially responsible firm. Johnson & Johnson's credo (see Figure 3.5) is one of the many ways in which social responsibility is emphasized at

Johnson & Johnson. As discussed in the following “Ethics in Action,” Johnson & Johnson’s ethical organizational culture provides the company and its various stakeholder groups with numerous benefits.



Ethics in Action

Johnson & Johnson’s Ethical Culture

Johnson & Johnson is so well known for its ethical culture that two years in a row a survey of over 26,000 consumers conducted by Harris Interactive and the Reputation Institute at New York University judged Johnson & Johnson to have the best corporate reputation.³⁷ Johnson & Johnson grew from a family business led by General Robert Wood Johnson in the 1930s to become a major maker of pharmaceutical and medical products. Attesting to the role of managers in creating ethical organizational cultures, Robert Wood Johnson emphasized the importance of ethics and responsibility to stakeholders and wrote the company’s first credo in 1943.³⁸

The credo continues to guide employees at Johnson & Johnson today and outlines the company’s commitments to its different stakeholder groups, emphasizing that the organization’s first responsibility is to doctors, nurses, patients, and consumers. Following this group are suppliers and distributors, employees, communities, and then stockholders.³⁹

The credo has served managers and employees at Johnson & Johnson well and guided some difficult decision making, such as the decision in 1982 to recall all Tylenol capsules in the U.S. market after cyanide-laced capsules were responsible for seven deaths in Chicago.

Consumer well-being always comes before profit considerations at Johnson & Johnson. Around 20 years ago, the harmful effects of sun exposure were much less well known by the public than they are today, and Johnson & Johnson’s baby oil was used as a tanning product.⁴⁰ The product manager for baby oil at the time, Carl Spalding, was making a presentation to top management about marketing



An employee removes Tylenol from a Chicago store’s shelves on Johnson & Johnson’s instructions after the discovery of contaminated supplies in 1982.

plans when Johnson & Johnson president David Clare mentioned that tanning might not be healthy.⁴¹ Before launching his planned marketing campaign, Spalding looked into the health issues related to tanning and discovered evidence suggesting health-related problems from too much exposure to the sun. Even though the evidence was not definitive, Spalding recommended that Johnson & Johnson no longer market baby oil as a tanning aid. This decision resulted in a 50 percent decrease in the company’s sales of baby oil, for a loss of \$5 million.⁴² The ethical values and norms in Johnson & Johnson’s culture, expressed in the credo, guide managers such as Carl Spalding to make the right decision in difficult situations.

An ethical culture and outstanding reputation bring other benefits to the organization in addition to helping employees make the right decisions. Jeanne Hamway, vice president for recruiting, finds that Johnson & Johnson's reputation facilitates the recruitment of new employees and attracts a diverse workforce.⁴³ Moreover, when organizations have an outstanding reputation, employees often are less tempted to act in a self-interested or unethical manner. Managers at Johnson & Johnson suggest that because company employees never accept bribes, the company is known as one in which bribes should not be offered.⁴⁴ All in all, ethical cultures like Johnson & Johnson's benefit various stakeholder groups in multiple ways.

The Increasing Diversity of the Workforce and the Environment

diversity Differences among people in age, gender, race, ethnicity, religion, sexual orientation, socioeconomic background, and capabilities/disabilities.

One of the most important management issues to emerge over the last 30 years has been the increasing diversity of the workforce. **Diversity** is dissimilarities—differences—among people due to age, gender, race, ethnicity, religion, sexual orientation, socioeconomic background, education, experience, physical appearance, capabilities/disabilities, and any other characteristic that is used to distinguish between people (see Figure 3.6).

Diversity raises important ethical issues and social responsibility issues. It is also a critical issue for organizations, one that if not handled well can bring an organization to its knees, especially in our increasingly global environment. There are several reasons why diversity is such a pressing concern and issue both in the popular press and for managers and organizations:

- There is a strong ethical imperative in many societies that diverse people receive equal opportunities and be treated fairly and justly. Unfair treatment is also illegal.
- Effectively managing diversity can improve organizational effectiveness.⁴⁵ When managers effectively manage diversity, they not only encourage other managers to treat diverse members of an organization fairly and justly but also realize that diversity is an important organizational resource that can help an organization gain a competitive advantage.
- There is substantial evidence that diverse individuals continue to experience unfair treatment in the workplace as a result of biases, stereotypes, and overt discrimination.⁴⁶ In one study, résumés of equally qualified men and women were sent to high-priced Philadelphia restaurants (where potential earnings are high). Though equally qualified, men were more than twice as likely as women to be called for a job interview and more than five times as likely to receive a job offer.⁴⁷ Findings from another study suggest that both women and men tend to believe that women will accept lower pay than men; this is a possible explanation for the continuing gap in pay between men and women.⁴⁸

Other kinds of diverse employees may face even greater barriers. For example, the federal Glass Ceiling Commission Report indicated that African-Americans have the hardest time being promoted and climbing the corporate ladder, that Asians are often stereotyped into technical jobs, and that Hispanics are assumed to

Figure 3.6
Sources of
Diversity in the
Workplace



glass ceiling A metaphor alluding to the invisible barriers that prevent minorities and women from being promoted to top corporate positions.

be less well educated than other minority groups.⁴⁹ (The term **glass ceiling** alludes to the invisible barriers that prevent minorities and women from being promoted to top corporate positions.)⁵⁰

Before we can discuss the multitude of issues surrounding the effective management of diversity, we must document just how diverse the U.S. workforce is becoming.

Age

According to the latest data from the U.S. Census Bureau, the median age of a person in the United States is the highest it has ever been, 35.3 years.⁵¹ Moreover, by 2030, it is projected that 20 percent of the population will be over 65.⁵² Title VII of the Civil Rights Act of 1964 and the Age Discrimination in Employment Act of 1967 are the major federal laws prohibiting age discrimination.⁵³ While we discuss federal employment legislation in more depth in Chapter 12, major equal employment opportunity legislation that prohibits discrimination among diverse groups is summarized in Table 3.2.

The aging of the population suggests managers need to be vigilant that employees are not discriminated against because of age. Moreover, managers need to ensure that the policies and procedures they have in place treat all workers fairly, regardless of their ages.

Gender

Women and men are almost equally represented in the U.S. workforce (approximately 53.5 percent of the U.S. workforce is male and 46.5 percent female),⁵⁴ yet women's median weekly earnings are estimated to be \$572 compared to \$714 for men.⁵⁵ Thus, the gender pay gap appears to be as alive and well as the glass ceiling. According to the nonprofit organization Catalyst, which studies women in business, while women comprise about 50.5 percent of the employees in managerial and

Table 3.2**Major Equal Employment Opportunity Laws Affecting Human Resources Management**

Year	Law	Description
1963	Equal Pay Act	Requires that men and women be paid equally if they are performing equal work.
1964	Title VII of the Civil Rights Act	Prohibits discrimination in employment decisions on the basis of race, religion, sex, color, or national origin; covers a wide range of employment decisions, including hiring, firing, pay, promotion, and working conditions.
1967	Age Discrimination in Employment Act	Prohibits discrimination against workers over the age of 40 and restricts mandatory retirement.
1978	Pregnancy Discrimination Act	Prohibits discrimination against women in employment decisions on the basis of pregnancy, childbirth, and related medical decisions.
1990	Americans with Disabilities Act	Prohibits discrimination against disabled individuals in employment decisions and requires that employers make accommodations for disabled workers to enable them to perform their jobs.
1991	Civil Rights Act	Prohibits discrimination (as does Title VII) and allows for the awarding of punitive and compensatory damages, in addition to back pay, in cases of intentional discrimination.
1993	Family and Medical Leave Act	Requires that employers provide 12 weeks of unpaid leave for medical and family reasons, including paternity and illness of a family member.

professional positions, only around 15.7 percent of corporate officers in the 500 largest U.S. companies (i.e., Fortune 500) are women, only 5.2 percent of the top earners are women, only 7.9 percent of those with the highest-ranking titles in corporate America are women (e.g., CEO or executive vice president), and only eight Fortune 500 companies have women as CEOs.⁵⁶ These women, such as Andrea Jung, CEO of Avon Products, and Carly S. Fiorina, CEO of Hewlett-Packard, stand out among their male peers and often receive a disparate amount of attention in the media. (We address this issue later, when we discuss the effects of being salient.) Women are also very underrepresented on boards of directors—they currently hold 13.6 percent of the board seats of Fortune 500 companies.⁵⁷ However, as Sheila Wellington, president of Catalyst, indicates, “Women either control or influence nearly all consumer purchases, so it’s important to have their perspective represented on boards.”⁵⁸

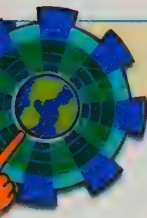
Additionally, research conducted by consulting firms suggests that female executives outperform their male colleagues on skills such as motivating others, promoting good communication, turning out high-quality work, and being a good listener.⁵⁹ For example, the Hagberg Group performed in-depth evaluations of 425 top executives in a variety of industries, with each executive rated by approximately 25 people. Of the 52 skills assessed, women received higher ratings than men on 42 skills, although at times the differences were small.⁶⁰ Results of a recent study conducted by Catalyst found that organizations with higher proportions of women in top-management positions had significantly better financial performance than organizations with lower proportions of female top managers.⁶¹ All in all,

studies such as these make one wonder why the glass ceiling continues to hamper the progress of women in business (a topic we address later in the chapter).

Race and ethnicity

The U.S. Census Bureau typically distinguishes between the following races: American Indian or Alaska Native (native Americans of origins in North, Central, or South America), Asian (origins in the Far East, Southeast Asia, or India), African-American (origins in Africa), Native Hawaiian or Pacific Islander (origins in the Pacific Islands such as Hawaii, Guam, and Samoa), and white (origins in Europe, the Middle East, or North Africa). While ethnicity refers to a grouping of people based on some shared characteristics such as national origin, language, or culture, the U.S. Census Bureau treats ethnicity in terms of whether a person is Hispanic or not Hispanic. Hispanics, also referred to as Latinos, are people whose origins are in Spanish cultures such as those of Cuba, Mexico, Puerto Rico, and South and Central America. Hispanics can be of different races.⁶² According to a recent poll, most Hispanics prefer to be identified by their country of origin (e.g., Mexican, Cuban, or Salvadoran) rather than by the overarching term *Hispanic*.⁶³

The racial and ethnic diversity of the U.S. population is increasing at an exponential rate, as is the composition of the workforce.⁶⁴ According to the U.S. Census in 2000, 75.1 percent of the population was white, 12.9 percent was African-American, 12.5 percent was Hispanic, and 3.6 percent was Asian.⁶⁵ Mexican-Americans are estimated to constitute over 60 percent of the U.S. Hispanic population, with the remainder of Hispanics having diverse countries of origin. As indicated in the following “Managing Globally,” the diversity of the U.S. population based on race and ethnicity will increase dramatically over the next few decades.



Managing Globally

Asians and Hispanics Projected to Be Fastest-Growing Group

According to projections released by the U.S. Census Bureau in the spring of 2004, the composition of the U.S. population in 2050 will be quite different from its composition in 2000. It is estimated that the Hispanic and Asian populations will triple during this 50-year period.⁶⁶ While the overall population in the United States is projected to grow from 282 million in 2000 to 419 million in 2050 (a 49 percent increase), estimated percentage growth rates for different ethnic and racial groups show that racial and ethnic diversity will definitely be on the rise.⁶⁷ Interestingly, while the U.S. population will increase by almost 50 percent in this next half-century, populations in many European countries are actually expected to decline.⁶⁸

Percentage growth rates for African-Americans, Asians, Hispanics (of any race), and other races are well above the overall population growth estimate, while the percentage growth rate for non-Hispanic whites is far below this figure.⁶⁹ More specifically, from 2000 to 2050, African-Americans, Asians, Hispanics (of any race), other races, and non-Hispanic whites have estimated growth rates of 71.3 percent, 212.9 percent, 187.9 percent, 217.1 percent, and 7.4 percent, respectively.⁷⁰



Puerto Rican Day Parade in New York City. It is estimated that the U.S. Hispanic and Asian populations will triple by 2050.

the population.⁷² All in all, these projections underscore the fact that the effective management of diversity in the workplace will only increase in importance in the years ahead.

The increasing racial and ethnic diversity of the workforce and the population as a whole underscores the importance of effectively managing diversity. Statistics compiled by the National Urban League suggest that much needs to be done in terms of ensuring that diverse employees are provided with equal opportunities. For example, African-Americans' earnings are approximately 73 percent of the earnings of whites,⁷³ and of 10,092 corporate officers in Fortune 500 companies, only 106 are African-American women.⁷⁴ In the remainder of this chapter, we focus on the fair treatment of diverse employees and explore why this is such an important challenge and what managers can do to meet it. We begin by taking a broader perspective and considering how increasing racial and ethnic diversity in an organization's environment (e.g., customers and suppliers) affects decision making and organizational effectiveness.

At a general level, managers and organizations are increasingly being reminded that stakeholders in the environment are diverse and expect organizational decisions and actions to reflect this diversity. For example, the NAACP (National Association for the Advancement of Colored People) and Children Now (an advocacy group) have lobbied the entertainment industry to increase the diversity in television programming, writing, and producing.⁷⁵ The need for such increased diversity is more than apparent. For example, while Hispanics make up 12.5 percent of the U.S. population (or 35 million potential TV viewers), only about 2 percent of the characters in prime-time TV shows are Hispanics (i.e., of the 2,251 characters in prime-time shows, only 47 are Hispanic), according to a study conducted by Children Now.⁷⁶ Moreover, only about 1.3 percent of the evening network TV news stories are reported by Hispanic correspondents, according to the Center for Media and Public Affairs.⁷⁷

Pressure is mounting on networks to increase diversity for a variety of reasons revolving around the diversity of the population as a whole, TV viewers, and consumers. For example, home and automobile buyers are increasingly diverse, reflecting the increasing diversity of the population as a whole.⁷⁸ Moreover, managers

In addition to experiencing increased racial and ethnic diversity, the U.S. population is also projected to get older. While the overall population growth rate is an estimated 48.8 percent, the segments of the population in the age groups of 45–64, 65–84, and 85 and over are expected to grow by 49.1 percent, 113.8 percent, and 388.9 percent, respectively.⁷¹ The U.S. Census Bureau made these projections based on Census 2000 data and assumptions regarding immigration patterns, mortality rates, and birth rates during the 2000–2050 period. For example, assumptions regarding immigration from China and India to the United States in the next several decades contribute to the projected high rate of growth in the Asian segment of

have to be especially sensitive to avoid stereotyping different groups when they communicate with potential customers. For example, Toyota Motor Sales USA made a public apology to the Reverend Jesse Jackson and his Rainbow Coalition for using a print advertisement depicting an African-American man with a Toyota RAV4 sport utility image embossed on his gold front tooth.⁷⁹

Religion

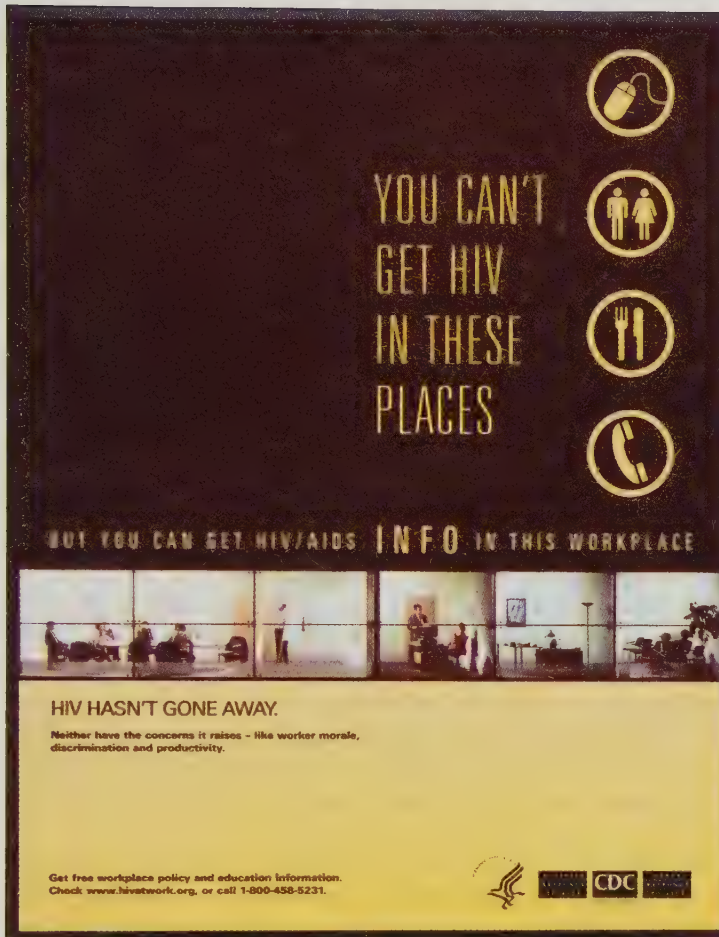
Title VII of the Civil Rights Act prohibits discrimination based on religion (as well as based on race/ethnicity, country of origin, and sex; see Table 5.1 and Chapter 12). In addition to enacting Title VII, in 1997 the federal government issued “The White House Guidelines on Religious Exercise and Expression in the Federal Workplace.”⁸⁰ These guidelines, while technically only applicable in federal offices, also are frequently relied on by large corporations. The guidelines require that employers make reasonable accommodations for religious practices such as observances of holidays as long as doing so does not entail major costs or hardships.⁸¹

A key issue for managers when it comes to religious diversity is recognizing and being aware of different religions and their beliefs, with particular attention being paid to when religious holidays fall. For example, critical meetings should not be scheduled during a holy day for members of a certain faith, and managers should be flexible in allowing people to have time off for religious observances. According to Lobna Ismail, director of a diversity training company in Silver Spring, Maryland, when managers acknowledge, respect, and make even small accommodations for religious diversity, employee loyalty is often enhanced. For example, allowing employees to leave work early on certain days instead of taking a lunch break or posting holidays for different religions on the company calendar can go a long way toward making individuals of diverse religions feel respected and valued as well as enable them to practice their faith.⁸²

Capabilities/Disabilities

The Americans with Disabilities Act (ADA) of 1990 prohibits discrimination against persons with disabilities and also requires that employers make reasonable accommodations to enable these people to effectively perform their jobs. In force for more than a decade, the ADA is not uncontroversial. On the surface, few would argue with the intent of this legislation. However, as managers attempt to implement policies and procedures to comply with the ADA, they face a number of interpretation and fairness challenges.

On the one hand, some people with real disabilities warranting workplace accommodations are hesitant to reveal their disabilities to their employers and claim the accommodations they deserve.⁸³ On the other hand, some employees abuse the ADA by seeking unnecessary accommodations for disabilities that may or may not exist.⁸⁴ Thus, it is perhaps not surprising that the passage of the ADA does not appear to have increased employment rates significantly for those with disabilities.⁸⁵ A key challenge for managers is to promote an environment in which employees needing accommodations feel comfortable disclosing their need and, at the same time, to ensure that the accommodations not only enable those with disabilities to effectively perform their jobs but also are perceived to be fair by those not disabled.⁸⁶ In addressing this challenge, often managers must educate both themselves and their employees about the disabilities, as well as the very real capabilities, of



One way managers can educate employees about HIV and AIDS is by hanging AIDS awareness posters in the workplace, such as the one depicted here.

those who are disabled. For example, during Disability Awareness Week 2004, administrators at the University of Notre Dame sought to increase the public's knowledge of disabilities while also heightening awareness of the abilities of persons who are disabled.⁸⁷ The University of Houston conducted a similar program called "Think Ability."⁸⁸ According to Cheryl Amoroso, director of the University of Houston's Center for Students with Disabilities, many people are unaware of the prevalence of disabilities as well as misinformed about their consequences. She suggests, for example, that although students may not be able to see, they can still excel in their coursework and have very successful careers.⁸⁹ Accommodations enabling such students to perform up to their capabilities are covered under the ADA.

The ADA also protects employees with acquired immune deficiency syndrome (AIDS) from being discriminated against in the workplace. AIDS is caused by the human immunodeficiency virus (HIV) and is transmitted through sexual contact, infected needles, and contaminated blood products. HIV is not spread through casual, nonsexual contact. Yet, out of ignorance, fear, or prejudice, some people wish to avoid all contact with anyone infected with HIV. Infected

individuals may not necessarily develop AIDS, and some individuals with HIV are able to remain effective performers of their jobs, while not putting others at risk.⁹⁰

AIDS awareness training can help people overcome their fears and also provide managers with a tool to prevent illegal discrimination against HIV-infected employees. Such training focuses on educating employees about HIV and AIDS, dispelling myths, communicating relevant organizational policies, and emphasizing the rights of HIV-positive employees to privacy and an environment that allows them to be productive.⁹¹ The need for AIDS awareness training is underscored by some of the problems HIV-positive employees experience once others in their workplace become aware of their condition.⁹² Moreover, organizations are required to make reasonable accommodations to enable people with AIDS to effectively perform their jobs.

Thus, managers have an obligation to educate employees about HIV and AIDS, dispel myths and the stigma of AIDS, and ensure that HIV-related discrimination is not occurring in the workplace. For example, Home Depot has provided HIV training and education to its store managers; such training was sorely needed given that over half of the managers indicated it was the first time they had the

opportunity to talk about AIDS.⁹³ Moreover, advances in medication and treatment mean that more infected individuals are able to continue working or are able to return to work after their condition improves.⁹⁴ Thus, managers need to ensure that these employees are fairly treated by all members of their organizations. And managers and organizations that do not treat HIV-positive employees in a fair manner, as well as provide reasonable accommodations (e.g., allowing time off for doctor visits or to take medicine), risk costly lawsuits.

Socioeconomic background

The term *socioeconomic background* typically refers to a combination of social class and income-related factors. From a management perspective, socioeconomic diversity (and, in particular, diversity in income levels) requires that managers be sensitive and responsive to the needs and concerns of individuals who might not be as well off as others. U.S. welfare reform in the mid- to late 1990s emphasized the need for single mothers and others receiving public assistance to join or return to the workforce. In conjunction with a strong economy, this led to record declines in the number of families, households, and children living below the poverty level, according to the 2000 U.S. census.⁹⁵ However, the economic downturn in the early 2000s, along with increased terrorism and the tragic collapse of the World Trade Center in New York City, resulted in domestic and international repercussions. These suggest that some past gains, which lifted families out of poverty, have been reversed. In a very strong economy, it is much easier for poor people with few skills to find jobs; in a weak economy, when companies lay off employees in hard times, people who need their incomes the most are unfortunately often the first to lose their jobs.⁹⁶

Even with all the gains from the 1990s, the U.S. Census Bureau estimates that 6,825,399 families had incomes below the poverty level in 2000, with 3,581,475 of these families being headed by single women.⁹⁷ The Census Bureau relies on predetermined threshold income figures, based on family size and composition, adjusted annually for inflation, to determine the poverty level. Families whose income falls below the threshold level are considered poor.⁹⁸ For example, in 2000 a family of four with two children under 18 was considered poor if their annual income fell below \$17,463.⁹⁹ When workers earn less than \$10 or \$15 per hour, it is often difficult, if not impossible, for them to meet their families' needs.¹⁰⁰ Moreover, increasing numbers of families are facing the challenge of finding suitable child care arrangements that enable the adults to work long hours and/or through the night to maintain an adequate income level. New information technology has led to more and more businesses operating 24 hours a day, creating real challenges for workers on the night shift, especially those with children.¹⁰¹

Hundreds of thousands of parents across the country are scrambling to find someone to care for their children while they are working the night shift, commuting several hours a day, working weekends and holidays, or putting in long hours on one or more jobs. This has led to the opening of day care facilities that operate around the clock as well as to managers seeking ways to provide such care for children of their employees. For example, the Children's Choice Learning Center in Las Vegas, Nevada, operates around the clock to accommodate employees working nights in neighboring casinos as cashiers and dealers as well as nurses, hospital workers, and call-center operators on the night shift. Randy Donahue, a security guard who works until midnight, picks his children up from the center when he gets

off work; his wife is a nurse on the night shift. There currently are five Children's Choice Learning Centers in the United States operating 24 hours a day, and plans are under way to add seven more.¹⁰²

Judy Harden, who focuses on families and child care issues for the United Workers Union, indicates that the demands families are facing necessitate around-the-clock and odd-hour child care options. Many parents simply do not have the choice of working at hours that allow them to take care of their children at night and/or on weekends, never mind when the children are sick.¹⁰³ In 1993, Ford Motor Company built an around-the-clock child care facility for 175 children of employees in Livonia, Michigan. However, a recent survey of child care needs indicates that many employees in other locations, such as Detroit and Kansas City, require such a facility. Some parents and psychologists feel uneasy having children separated from their families for so much time and particularly at night. Most agree that unfortunately for many families this is not a choice but a necessity.¹⁰⁴

Socioeconomic diversity suggests that managers need to be sensitive and responsive to the needs and concerns of workers who may be less fortunate than themselves in terms of income and financial resources, child care and elder care options, housing opportunities, and existence of sources of social and family support. Moreover—and equally important—managers should try to provide such individuals with opportunities to learn, advance, and make meaningful contributions to their organizations while improving their economic well-being.

Sexual orientation

Approximately 2 to 6 percent of the U.S. population is gay or lesbian.¹⁰⁵ While no federal law prohibits discrimination based on sexual orientation, 14 states have such laws, and a 1998 executive order prohibits sexual orientation discrimination in civilian federal offices. Moreover, an increasing number of organizations recognize the minority status of gay and lesbian employees, affirm their rights to fair and equal treatment, and provide benefits to same-sex partners of gay and lesbian employees. For example, 95 percent of Fortune 500 companies prohibit discrimination based on sexual orientation, and 70 percent of the Fortune 500 companies provide domestic-partner benefits.¹⁰⁶ As indicated in the following "Focus on Diversity," there are many steps that managers can take to ensure that sexual orientation is not used to unfairly discriminate among employees.



Focus on Diversity

Gays and Lesbians in the Workplace

While gays and lesbians have made great strides in terms of attaining fair treatment in the workplace, much more needs to be done. In a recent study conducted by Harris Interactive Inc. (a research firm) and Witeck Communications Inc. (a marketing firm), over 40 percent of gay and lesbian employees indicated that they had been unfairly treated, denied a promotion, or pushed to quit their jobs because of their sexual orientation.¹⁰⁷ Given continued harassment and discrimination despite the progress that has been made,¹⁰⁸ many gay and lesbian employees fear disclosing their sexual orientation in the workplace and thus live a life of secrecy. While there are a few openly gay top managers, such as David Geffen, cofounder of DreamWorks SKG, and Allan Gilmour, vice chairman of

Ford, many others choose not to disclose or discuss their personal lives, including long-term partners.¹⁰⁹

Thus, it is not surprising that many managers are taking active steps to educate and train their employees in regard to issues of sexual orientation. S. C. Johnson & Sons, Inc., maker of Raid insecticide and Glade air fresheners in Racine, Wisconsin, provides mandatory training to its plant managers to overturn stereotypes, as does Eastman Kodak. Other organizations such as Lucent Technologies, Microsoft, and Southern California Edison send employees to seminars conducted at prominent business schools such as the Anderson School of Management at the University of California, Los Angeles. Companies like Raytheon, IBM, Eastman Kodak, and Lockheed Martin provide assistance to their gay and lesbian employees through gay and lesbian support groups.¹¹⁰

More generally, the presence of a gay, lesbian, bisexual, and transgender (GLBT) rights movement in the workplace is steadily increasing. From an individual employee perspective, sometimes these rights boil down to receiving the same kind of treatment as one's heterosexual co-workers. For example, when Daniel Kline applied to use United Parcel Service's Management Initiated Transfer to follow his partner of 27 years to another state, he was initially denied. This program allows employees to transfer to UPS offices in other states and retain their seniority when the employee's spouse accepts a job in another state. Kline's partner was transferred from United Parcel's office in San Francisco to its office in Chicago, and Kline was hoping to remain with UPS when he, too, moved to Chicago. After Kline took his case to the Lambda Legal Defense and Education Fund, a GLBT advocacy organization, and threatened legal action based on California's antidiscrimination laws, UPS reversed its position and allowed the transfer.¹¹¹

Clearly, many highly qualified potential and current employees might happen to be gay or lesbian. An organization that does not welcome and support such employees not only is unfairly discriminating against this group but also is losing the contributions of valued potential employees. Additionally, an organization that discriminates against this group risks alienating customers. Fifteen million consumers are in the GLBT group in the United States, and according to research conducted by MarketResearch.com, their purchasing power is around \$485 billion.¹¹²

Other kinds of diversity

There are other kinds of diversity that are important in organizations, critical for managers to deal with effectively, and also potential sources of unfair treatment. For example, organizations and teams need members with diverse backgrounds and experiences. This is clearly illustrated by the prevalence of cross-functional teams in organizations whose members might come from various departments such as marketing, production, finance, and sales (teams are covered in depth in Chapter 11). A team responsible for developing and introducing a new product, for example, often will need the expertise of employees not only from R&D and engineering but also from marketing, sales, production, and finance.

Other types of diversity can also affect how employees are treated in the workplace. For example, employees differ from each other in how attractive they are [based on the standards of the culture(s) in which an organization operates] and in terms of body weight. Whether individuals are attractive or thin or unattractive or

overweight, in most cases, has no bearing on their job performance unless they have jobs in which physical appearance plays a role, such as modeling. Yet sometimes these physical sources of diversity end up influencing advancement rates and salaries. For example, a recent study published in the *American Journal of Public Health* found that highly educated obese women earned approximately 30 percent less per year than women who were not obese and men (regardless of whether or not the men were obese).¹¹³ Clearly, managers need to ensure that all employees are treated fairly, regardless of their physical appearance.

Managers and the Effective Management of Diversity

The increasing diversity of the environment—which, in turn, increases the diversity of an organization's workforce—increases the challenges managers face in effectively managing diversity. Each of the eight kinds of diversity discussed above presents managers with a particular set of issues they need to appreciate before they can respond to them effectively. Understanding these issues is not always a simple matter, as many informed managers have discovered. Research on how different groups are currently treated and the unconscious biases that might adversely affect them is critical because it helps managers become aware of the many subtle and unobtrusive ways in which diverse employee groups can come to be treated unfairly over time. There are many more steps managers can take to become sensitive to the ongoing effects of diversity in their organizations, take advantage of all the contributions diverse employees can make, and prevent diverse employees from being unfairly treated.

Critical managerial roles

In each of their managerial roles (see Chapter 1), managers can either promote the effective management of diversity or derail such efforts; thus, they are critical to this process. For example, in their interpersonal roles, managers can convey that the effective management of diversity is a valued goal and objective (figurehead role), can serve as a role model and institute policies and procedures to ensure that diverse organizational members are treated fairly (leader role), and can enable diverse individuals and groups to coordinate their efforts and cooperate with each other both inside the organization and at the organization's boundaries (liaison role). In Table 3.3 we summarize some of the ways in which managers can ensure that diversity is effectively managed as they perform their different roles.

Given the formal authority that managers have in organizations, they typically have more influence than rank-and-file employees. When managers commit to supporting diversity, their authority and positions of power and status influence other members of an organization to make a similar commitment.¹¹⁴ Research on social influence supports such a link, as people are more likely to be influenced and persuaded by others who have high status.¹¹⁵

Moreover, when managers commit to diversity, their commitment legitimizes the diversity management efforts of others.¹¹⁶ In addition, resources are devoted to such efforts and all members of an organization believe that their diversity-related efforts are supported and valued. Consistent with this reasoning, top-management commitment and rewards for the support of diversity are often cited

Table 3.3
Managerial Roles and the Effective Management of Diversity

Type of Role	Specific Role	Example
Interpersonal	Figurehead	Convey that the effective management of diversity is a valued goal and objective.
	Leader	Serve as a role model and institute policies and procedures to ensure that diverse members are treated fairly.
	Liaison	Enable diverse individuals to coordinate their efforts and cooperate with one another.
Informational	Monitor	Evaluate the extent to which diverse employees are being treated fairly.
	Disseminator	Inform employees about diversity policies and initiatives and the intolerance of discrimination.
	Spokesperson	Support diversity initiatives in the wider community and speak to diverse groups to interest them in career opportunities.
Decisional	Entrepreneur	Commit resources to develop new ways to effectively manage diversity and eliminate biases and discrimination.
	Disturbance handler	Take quick action to correct inequalities and curtail discriminatory behavior.
	Resource allocator	Allocate resources to support and encourage the effective management of diversity.
	Negotiator	Work with organizations (e.g., suppliers) and groups (e.g., labor unions) to support and encourage the effective management of diversity.

as critical ingredients for the success of diversity management initiatives.¹¹⁷ Additionally, seeing managers express confidence in the abilities and talents of diverse employees causes other organizational members to be similarly confident and helps to reduce any misconceived misgivings they may have as a result of ignorance or stereotypes.¹¹⁸

Another important reason that managers are so central to the effective management of diversity hinges on two factors. The first factor is that women, African-Americans, Hispanics, and other minorities often start out at a slight disadvantage due to the ways in which they are perceived by others in organizations, particularly in work settings where they are a numerical minority. As Virginia Valian, a psychologist at Hunter College who studies gender, indicates, “In most organizations women begin at a slight disadvantage. A woman does not walk into the room with the same status as an equivalent man, because she is less likely than a man to be viewed as a serious professional.”¹¹⁹


The second factor is that research suggests slight differences in treatment can cumulate and result in major disparities over time. Even small differences—such as a very slight favorable bias toward men for promotions—can lead to major differences in the number of male and female managers over time.¹²⁰ Thus, while women and other minorities are sometimes advised not to make “a mountain out of a molehill” when they perceive they have been unfairly treated, research conducted by Valian and others suggests that molehills (i.e., slight differences in treatment based on irrelevant distinctions such as race, gender, or ethnicity) can turn into mountains over

time (i.e., major disparities in important outcomes such as promotions) if they are ignored.¹²¹ Once again, managers play a crucial role in ensuring that neither large nor small disparities in treatment and outcomes due to irrelevant distinctions such as race or ethnicity occur in organizations. Moreover, managers have the obligation, from both an ethical and a business perspective, to ensure that such disparities do not occur and are not tolerated in organizations.

Effectively managing diversity makes good business sense

The diversity of organizational members can be a source of competitive advantage, helping an organization provide customers with better goods and services.¹²² The variety of points of view and approaches to problems and opportunities that diverse employees provide can improve managerial decision making. Suppose the Budget Gourmet frozen-food company is trying to come up with some creative ideas for new frozen meals that will appeal to health-conscious, time-conscious customers tired of the same old frozen-food fare. Which group do you think is likely to come up with the most creative ideas: a group of white women with master's degrees in marketing from Yale University who grew up in upper-middle-class families in the Northeast or a racially mixed group of men and women who grew up in families with varying income levels in different parts of the country and attended a mix of business schools (New York University, Oklahoma State, University of Michigan, UCLA, Cornell University, Texas A&M University, and Iowa State)? Most people would agree that the diverse group is likely to come up with a wider range of creative ideas. Although this example is simplistic, it underscores one way in which diversity can lead to a competitive advantage.

Just as the workforce is becoming increasingly diverse, so too are the customers who buy an organization's goods or services. In an attempt to suit local customers' needs and tastes, managers of Target's chain of 623 discount stores vary the selection of products available in stores in different cities and regions. For example, the Target store in Phoenix, Arizona, stocks religious candles and Spanish-language diskettes and Disney videos to appeal to local Hispanic Catholics; the Target store in Scottsdale, Arizona, stocks in-line skates and bicycle baby trailers that appeal to well-to-do yuppies.¹²³ In some large cities such as Houston, Texas, Hispanic immigrants have created communities of businesses that cater to diverse customers, as highlighted in the following "Manager as a Person."



Manager as a Person

Creating a Business Through Sheer Determination

In Houston, Texas, there are over 500 businesses that have been founded by immigrants to serve diverse customers and clients.¹²⁴ Often, these immigrants arrived in the city with little else but their will and determination. Take the case of Jose Camarena, who started working at the age of 10 in Mexico City and came to the United States in 1978 with his wife. After working in restaurants in Chicago for a few years, Camarena decided in the early 1980s to move to Houston and open a restaurant.¹²⁵ Camarena realized there were actually few Mexican fast-food restaurants in the city, and fast food became the niche of his

restaurant, Taqueria Arandas.¹²⁶ The restaurant was so popular that Camarena was able to open seven more restaurants within 10 years and now sells Taqueria Arandas franchises. Taqueria Arandas now has 27 franchised Taquerias as well as two seafood restaurants and four Arandas bakeries. Camarena's belief in the value of hard work and his determination to succeed underlie the growth of his business. With a successful company earning \$36 million in annual revenues and employing 900 employees, Camarena has not slowed down and continues to put in a full day's work. As he puts it, "I love to work . . . Lazy people, it doesn't go well for them."¹²⁷

Similar success stories are found among other entrepreneurs in Houston who started businesses from scratch in Hispanic communities. Cesar Rodriguez, who arrived in Houston with his mother and brothers in 1973, lived in a run-down boarding house, and took whatever odd jobs he could find, ranging from cleaning offices to busing restaurant tables to help out his family.¹²⁸

After a year of working at these jobs, Rodriguez received an income tax refund from the IRS for \$600. Even though he didn't own a car or a home, he decided to use his tax refund to open a restaurant serving tacos, shrimp cocktails, margaritas, and other delicacies that appealed to his then mainly Hispanic customers. Doneraki, as the restaurant was called, grossed \$1 million in sales its first year. Today, Doneraki operates four successful restaurants with combined revenues of about \$12 million and 300 employees.¹²⁹ Moreover, its restaurants appeal to all kinds of customers in diverse neighborhoods. Rodriguez's success story illustrates how entrepreneurs and managers who are driven to succeed can overcome what might seem to others to be insurmountable odds.



Jose Camarena's determination helped him create his successful Mexican fast-food restaurant, Taquerias Arandas.

Diverse members of an organization are likely to be attuned to what goods and services diverse segments of the market want and do not want. Major car companies, for example, are increasingly assigning women to their design teams to ensure that the needs and desires of female customers (a growing segment of the market) are taken into account in new car design.

For Darden Restaurants, the business case for diversity rests on market share and growth. Darden seeks to satisfy the needs and tastes of diverse customers by providing menus in Spanish in communities with large Hispanic populations.¹³⁰ Similarly, market share and growth and the identification of niche markets led Tracey Campbell to cater to travelers with disabilities.¹³¹ She heads InnSeekers, a telephone and online listing resource for bed and breakfasts. Nikki Daruwala works for the Calvert Group in Bethesda, Maryland, a mutual fund that emphasizes social responsibility and diversity. She indicates that profit alone is more than enough of an incentive to effectively manage diversity. As she puts it, "You can look at an

automaker. There are more women making decisions about car buying or home buying . . . \$3.72 trillion per year are spent by women.”¹³²

Another way in which the effective management of diversity can positively affect profitability is that it increases retention of valued employees, which decreases the costs of hiring replacements for those who quit as well as ensures that all employees are highly motivated. In terms of retention, given the current legal environment, more and more organizations are attuned to the need to emphasize the importance of diversity in hiring. Once hired, if diverse employees think they are being unfairly treated, however, they will be likely to seek opportunities elsewhere. Thus, the recruiting of diverse employees has to be followed up by the ongoing effective management of diversity to retain these valued organizational members.

If diversity is not effectively managed and results in turnover rates being higher for members of certain groups who are not treated fairly, profitability will suffer on several counts. Not only are the future contributions of diverse employees lost when they quit, but the organization also has to bear the costs of hiring replacement workers. According to the Employment Management Association, on average it costs more than \$10,000 to hire a new employee; other estimates are significantly higher. For example, Ernst & Young estimates it costs about \$1,200,000 to replace 10 professionals, and the diversity consulting firm Hubbard & Hubbard estimates replacement costs average one-and-a-half times an employee's annual salary.¹³³ Moreover, additional costs from failing to effectively manage diversity stem from time lost due to the barriers diverse members of an organization perceive as thwarting their progress and advancement.¹³⁴

Effectively managing diversity makes good business sense for another reason. More and more, managers and organizations concerned about diversity are insisting that their suppliers also support diversity. Managers of American Airlines, for example, recently announced that all the law firms they hire must submit quarterly reports indicating the extent to which diverse employees worked on the airline's account. Similarly, managers at Chrysler, Aetna Life & Casualty, and General Motors all consider information about the extent to which law firms support diversity when they are deciding which law firms will represent them.¹³⁵ Managers in the Teachers Insurance and Annuity Association-College Retirement Equities Fund (TIAA-CREF) are putting pressure on Nucor Corporation to add women and minorities to its board of directors, which currently consists entirely of white men. TIAA-CREF owns 912,900 shares in Nucor, and its managers believe that their heavy investment in Nucor gives them enough clout to bring diversity to the board of directors.¹³⁶

Finally, from both a business and an ethical perspective, the effective management of diversity is necessary to avoid costly lawsuits such as those settled by Advantica (owner of the Denny's chain) and the Coca-Cola Company. Recently Coca-Cola settled a class-action suit brought by African-American employees, at a cost of \$192 million. The damage such lawsuits cause goes beyond the monetary awards to the injured parties; it can tarnish a company's image. One positive outcome of Coca-Cola's recent settlement is the company's recognition of the need to commit additional resources to diversity management initiatives. In this regard, Coca-Cola is increasing its use of minority suppliers, instituting a formal mentoring program, and instituting days to celebrate diversity with its workforce.¹³⁷ By now, it should be clear that effectively managing diversity is a necessity on both ethical and business grounds.

Sexual Harassment

Sexual harassment seriously damages both the people who are harassed and the reputation of the organization in which it occurs. It also can cost organizations large amounts of money. In 1995, for example, Chevron

Corporation agreed to pay \$2.2 million to settle a sexual harassment lawsuit filed by four women who worked at the Chevron Information Technology Company in San Ramon, California. One woman involved in the suit said that she had received violent pornographic material through the company mail. Another, an electrical engineer, said that she had been asked to bring pornographic videos to Chevron workers at an Alaska drill site.¹³⁸ More recently, TWA settled a lawsuit to the tune of \$2.6 million that alleged that female employees were sexually harassed at JFK International Airport in New York. According to the EEOC, not only was sexual harassment tolerated at TWA, but also company officials did little to curtail it when it was brought to their attention.¹³⁹

Unfortunately, the events at Chevron and TWA are not isolated incidents.¹⁴⁰ Sixty percent of the 607 women surveyed by the National Association for Female Executives indicated that they had experienced some form of sexual harassment.¹⁴¹ Sexual harassment victims can be women or men, and their harassers do not necessarily have to be of the opposite sex.¹⁴² However, women are the most frequent victims of sexual harassment, particularly those in male-dominated occupations or those who occupy positions stereotypically associated with certain gender relationships, such as a female secretary reporting to a male boss. Though it occurs less frequently, men can also be victims of sexual harassment. For instance, several male employees at Jenny Craig filed a lawsuit claiming that they were subject to lewd and inappropriate comments from female co-workers and managers.¹⁴³ Sexual harassment is not only unethical; it is also illegal. Managers have an ethical obligation to ensure that they, their co-workers, and their subordinates never engage in sexual harassment, even unintentionally.

Forms of sexual harassment

There are two basic forms of sexual harassment: quid pro quo sexual harassment and hostile work environment sexual harassment. **Quid pro quo sexual harassment** occurs when a harasser asks or forces an employee to perform sexual favors to keep a job, receive a promotion, receive a raise, obtain some other work-related opportunity, or avoid receiving negative consequences such as demotion or dismissal.¹⁴⁴ This “Sleep with me, honey, or you’re fired” form of harassment is the more extreme type and leaves no doubt in anyone’s mind that sexual harassment has taken place.¹⁴⁵

Hostile work environment sexual harassment is more subtle. It occurs when organizational members are faced with an intimidating, hostile, or offensive work environment because of their sex.¹⁴⁶ Lewd jokes, sexually oriented comments or innuendos, vulgar language, displays of pornography, displays or distribution of sexually oriented objects, and sexually oriented remarks about one’s physical appearance are examples of hostile work environment sexual harassment.¹⁴⁷ A hostile work environment interferes with organizational members’ ability to perform their jobs effectively and has been deemed illegal by the courts. Managers who engage in hostile work environment harassment or allow others to do so risk costly lawsuits for their organizations.

quid pro quo sexual harassment

Asking for or forcing an employee to perform sexual favors in exchange for some reward or to avoid negative consequences.

hostile work environment sexual harassment

Telling lewd jokes, displaying pornography, making sexually oriented remarks about someone’s personal appearance, and other sex-related actions that make the work environment unpleasant.

Steps managers can take to eradicate sexual harassment

Managers have an ethical obligation to eradicate sexual harassment in their organizations. There are many ways to accomplish this objective. Here are four initial steps that managers can take to deal with the problem.¹⁴⁸

- ✱ *Develop and clearly communicate a sexual harassment policy endorsed by top management.* This policy should include prohibitions against both quid pro quo and hostile work environment sexual harassment. It should contain (1) examples of types of behavior that are unacceptable, (2) a procedure for employees to use to report instances of harassment, (3) a discussion of the disciplinary actions that will be taken when harassment has taken place, and (4) a commitment to educate and train organizational members about sexual harassment.
- ✱ *Use a fair complaint procedure to investigate charges of sexual harassment.* Such a procedure should (1) be managed by a neutral third party, (2) ensure that complaints are dealt with promptly and thoroughly, (3) protect and fairly treat victims, and (4) ensure that alleged harassers are fairly treated.
- ✱ *When it has been determined that sexual harassment has taken place, take corrective actions as soon as possible.* These actions can vary depending on the severity of the harassment. When harassment is extensive, prolonged over a period of time, of a quid pro quo nature, or severely objectionable in some other manner, corrective action may include firing the harasser.
- ✱ *Provide sexual harassment education and training to all organizational members, including managers.* The majority of Fortune 500 firms currently provide this education and training for their employees. Managers at Du Pont, for example, developed Du Pont's "A Matter of Respect" program to help educate employees about sexual harassment and eliminate its occurrence. The program includes a four-hour workshop in which participants are given information that defines sexual harassment, sets forth the company's policy against it, and explains how to report complaints and access a 24-hour hotline. Participants watch video clips showing actual instances of harassment. One clip shows a saleswoman having dinner with a male client who, after much negotiating, seems about to give her company his business when he suddenly suggests that they continue their conversation in his hotel room. The saleswoman is confused about what to do. Will she be reprimanded if she says no and the deal is lost? After watching a video, participants discuss what they have seen, why the behavior is inappropriate, and what organizations can do to alleviate the problem.¹⁴⁹ Throughout the program, managers stress to employees that they do not have to tolerate sexual harassment or get involved in situations in which harassment is likely to occur.

Barry S. Roberts and Richard A. Mann, experts on business law and authors of several books on the topic, suggest a number of additional factors that managers and all members of an organization need to keep in mind about sexual harassment:¹⁵⁰

- ✱ Every sexual harassment charge should be taken very seriously.
- ✱ Employees who go along with unwanted sexual attention in the workplace can be sexual harassment victims.

- Employees sometimes wait before they file complaints of sexual harassment.
- An organization's sexual harassment policy should be communicated to each new employee and reviewed with current employees on a periodic basis.
- Suppliers and customers need to be familiar with an organization's sexual harassment policy.
- Managers should provide employees with alternative ways to report incidents of sexual harassment.
- Employees who report sexual harassment must have their rights protected; this includes being protected from any potential retaliation.
- Allegations of sexual harassment should be kept confidential; those accused of harassment should have their rights protected.
- Investigations of harassment charges and any resultant disciplinary actions need to proceed in a very timely manner.
- Managers must protect employees from sexual harassment from any third-party employees they may interact with in the course of performing their jobs, such as suppliers or customers.¹⁵¹

Summary and Review

ETHICS AND STAKEHOLDERS Ethics are moral principles or beliefs about what is right or wrong. These beliefs guide people in their dealings with other individuals and groups (stakeholders) and provide a basis

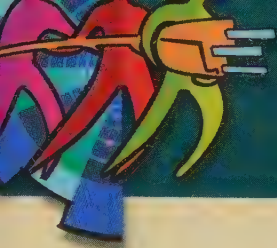
for deciding whether behavior is right and proper. Many organizations have a formal code of ethics derived primarily from societal ethics, professional ethics, and the individual ethics of the organization's top managers. Managers can apply ethical standards to help themselves decide on the proper way to behave toward organizational stakeholders. Ethical organizational cultures are those in which ethical values and norms are emphasized. Ethical organizational cultures can help organizations and their members behave in a socially responsible manner.

INCREASING DIVERSITY OF WORKFORCE AND ENVIRONMENT

Diversity is differences among people due to age, gender, race, ethnicity, religion, sexual orientation, socioeconomic background, and capabilities/disabilities. The workforce and the organizational environment have become increasingly diverse. Effectively managing diversity is an ethical imperative and can improve organizational effectiveness.

MANAGING DIVERSITY The effective management of diversity is not only an essential responsibility of managers but an ethical and a business imperative. In each of their managerial roles, managers can encourage organizationwide acceptance and valuing of diversity.

SEXUAL HARASSMENT Two forms of sexual harassment are quid pro quo sexual harassment and hostile work environment sexual harassment. Steps that managers can take to eradicate sexual harassment include development, communication, and enforcement of a sexual harassment policy, use of fair complaint procedures, prompt corrective action when harassment occurs, and sexual harassment training and education.



Management in Action

Topics for Discussion and Action

Discussion

1. When are ethics and ethical standards especially important in organizations?
2. Why might managers do things that conflict with their own ethical values?
3. How can managers ensure that they create ethical organizational cultures?

4. Why are gay and lesbian workers and workers who test positive for HIV sometimes discriminated against?
5. Why might some employees resent workplace accommodations that are dictated by the Americans with Disabilities Act?

Action

6. Choose a Fortune 500 company not mentioned in the chapter. Conduct research to determine what steps this organization has taken to effectively manage diversity and eliminate sexual harassment.

Building Management Skills

Solving Diversity-Related Problems

Think about the last time that you (1) were treated unfairly because you differed from a decision maker on a particular dimension of diversity or (2) observed someone else being treated unfairly because that person differed from a decision maker on a particular dimension of diversity. Then answer these questions:

1. Why do you think the decision maker acted unfairly in this situation?
2. In what ways, if any, were biases, stereotypes, or overt discrimination involved in this situation?
3. Was the decision maker aware that he or she was acting unfairly?
4. What could you or the person who was treated unfairly have done to improve matters and rectify the injustice on the spot?
5. Was any sexual harassment involved in this situation? If so, what kind was it?
6. If you had authority over the decision maker (e.g., if you were his or her manager or supervisor), what steps would you take to ensure that the decision maker no longer treated diverse individuals unfairly?

Small Group Breakout Exercise

Determining If a Problem Exists

Form groups of three or four people, and appoint one member as the spokesperson who will communicate your findings to the whole class when called on by the instructor. Then discuss the following scenario.

You and your partners own and manage a local chain of restaurants, with moderate to expensive prices, that are open for

lunch and dinner during the week and for dinner on weekends. Your staff is diverse, and you believe that you are effectively managing diver-

sity. Yet on visits to the different restaurants you have noticed that your African-American employees tend to congregate together and

communicate mainly with each other. The same is true for your Hispanic employees and your white employees. You are meeting with your partners today to discuss this observation.


1. Discuss why the patterns of communication that you

observed might be occurring in your restaurants.

2. Discuss whether your observation reflects an underlying problem. If so, why? If not, why not?

3. Discuss whether you should address this issue with your staff and in your restaurants. If so, how and why? If not, why not?

Be the Manager



You are Maria Herrera and have been recently promoted to the position of director of financial analysis for a medium-size consumer goods firm. During your first few weeks on the job, you took the time to have lunch with each of your subordinates to try to get to know them better. You have 12 direct reports who are junior and senior financial analysts who support different product lines. Susan Epstein, one of the female financial analysts you had

lunch with, made the following statement, "I'm so glad we finally have a woman in charge. Now, hopefully things will get better around here." You pressed Epstein to elaborate, but she clammed up. She indicated that she didn't want to unnecessarily bias you and that the problems were pretty self-evident. In fact, Epstein was surprised that you didn't know what she was talking about and jokingly mentioned that perhaps you should spend some time under-


cover, observing her group and their interactions with others.

You spoke with your supervisor and the former director who had been promoted and had volunteered to be on call if you had any questions. Neither man knew of any diversity-related issues in your group. In fact, your supervisor's response was, "We've got a lot of problems, but fortunately that's not one of them." What are you going to do to address this issue?



Additional Activities on the Build Your Management Skills DVD

- **Test Your Knowledge:**
(1) Ethics, (2) Comparing Affirmative Action, Valuing Diversity, and Managing Diversity, (3) Mentoring, and (4) International Cultural Diversity
- **Self-Assessment:**
(1) Assessing Your Ethical Decision-Making Skills and (2) Appreciating and Valuing Diversity
- **Manager's Hot Seat:**
(1) Ethics: Let's Make a Fourth Quarter Deal and (2) Office Romance: Grouping for Answers



Managing Ethically

Some companies require that their employees work very long hours and travel extensively. Employees with young children,

employees taking care of elderly relatives, and employees who have interests outside the workplace sometimes find that their careers

are jeopardized if they try to work more reasonable hours or limit their work-related travel. Some of these employees feel that it is unethical

for their manager to expect so much of them in the workplace and not understand their needs as parents and caregivers.

Questions

1. Either individually or in a group, think about the ethical

implications of requiring long hours and extensive amounts of travel for some jobs.

2. What obligations do you think managers and companies

have to enable employees to have a balanced life and meet nonwork needs and demands?

BusinessWeek

Case in the News

Investors in embattled American International Group Inc. may have breathed a sigh of relief at the March 28 announcement that Chairman Maurice R. “Hank” Greenberg would step aside two weeks after being pressured to give up the chief executive’s role. But the complex \$99 billion insurance and financial empire he leaves behind remains mired in turmoil.

What began as an investigation into two reinsurance transactions has mushroomed into a growing scandal that has tarnished the reputation of one of America’s premier corporations. On March 30, AIG acknowledged that it had improperly accounted for the reinsurance transaction to bolster reserves, and detailed numerous other examples of problematic accounting. It also announced the delay of its annual 10-K filing, and said the moves may have inflated its net worth by up to \$1.7 billion. While AIG says it does not yet know if the review will force a restatement of prior results, its stock dropped 2.1 percent on the news; all together, AIG shares have dropped 22 percent, to \$57 apiece, since the company was served with subpoenas by state and federal

regulators six weeks ago. The announcement also caused Standard & Poor’s to downgrade AIG’s debt rating from AAA to AA+. Here’s a look at where the AIG mess stands and where the probes are headed:

What Is It That Has Regulators Up in Arms?

Investigators believe that AIG may have goosed its financial performance with dubious transactions and improper accounting. Last fall, the insurer paid \$126 million in fines to the Securities & Exchange Commission and Justice Department for deals it structured for outside clients that allegedly violated insurance accounting rules, although AIG admitted no wrongdoing. The company also came under the glare of New York Attorney General Eliot Spitzer for its role in bid-rigging with broker Marsh & McLennan Cos., which led to the ouster of Hank’s son Jeffrey as CEO there. AIG admitted no wrongdoing, but two of its executives pled guilty and left the company.

This time, investigators initially focused on two transactions involv-

AIG: What Went Wrong

ing Berkshire Hathaway’s General Re Corporation unit. The deals essentially amounted to a \$500 million loan that was dressed up on the books as premium revenue. That allowed AIG to boost its sagging reserves at a time when investors thought they were too low. The problem: AIG never assumed any of the risk associated with insurance underwriting. On March 30, the company acknowledged that “the transaction documentation was improper” and should never have been classified as insurance premiums.

Since then, AIG’s problems have escalated. In its March 30 release, the company itself identified several problem areas. They include transactions with supposedly independent companies that were in fact controlled by AIG; bond transactions that may have allowed it to claim gains without actually selling the bonds; misclassified losses; and questionable estimates on deferred acquisition costs. Investigators and state regulators are looking into some 60 transactions involving these and other possible accounting shenanigans. “Greenberg strived for a steadily rising stock price,” says a source in

Spitzer's office. "He used mechanisms now being revealed as deceptive and improper."

What Is the Company Doing at This Point?

It has installed longtime AIG executive Martin J. Sullivan, 50, as the new CEO, and named independent director Frank G. Zarb as chairman. In addition, it has launched its own internal investigation, which has so far revealed several arrangements and deals that were not properly accounted for. The company says that its review is not yet complete. Moreover, AIG has pledged to change how it accounts for deferred compensation that's now paid to senior executives through Starr International Co. (SICO)—one of several controversial private entities that also are under investigation.

What Are These Private Entities and Why Are They Under Scrutiny?

AIG has a highly unusual arrangement with three private entities, governed and controlled by Greenberg and other AIG executives. Each serves a different purpose and raises unique concerns. SICO is a holding company that owns about 12 percent of AIG stock—making it the company's largest shareholder—and pays out some of that stock to an elite group of AIG managers as deferred compensation. Greenberg and other AIG directors sit on the board, have large personal stakes, and decide who gets paid what. Regulators believe SICO hides executive pay and takes away powers that should rightly lie with the compensation committee of the board.

C.V. Starr & Co., on the other hand, is a group of agencies that develops business and issues specialized policies for AIG. It's owned and operated by AIG executives—many of whom perform functions similar to what they do at AIG—and controls 1.8 percent of AIG shares. Critics worry that the opaque nature of its transactions, for example, could allow C.V. Starr to become a convenient tool for managing earnings at AIG, which has been a model of earnings consistency in a notoriously volatile industry. The arrangement also creates endless possibilities for conflicts of interest. Says North Carolina State Treasurer Richard H. Moore, who oversees a stake in AIG worth more than \$300 million: "I don't think you can have a publicly traded company that allows board members to own a private entity that does business with the publicly traded company. [It's] impossible to know if shareholders are being taken advantage of."

Finally, there's the Starr Foundation, a charitable entity which Greenberg also chairs and which has a 2 percent share in AIG. It has come under fire for doling out money for political causes and for giving \$36.5 million to the American Museum of Natural History shortly after museum President Ellen V. Futter joined AIG's board.

What Pressure Does Sullivan Now Face?

Insiders say the new chief, who began his AIG career at the age of 16, is aggressively leading the charge for changes necessary to create a more transparent organization. But the longtime AIG manager—formerly a vice-chairman and co-chief operating officer—is also under scrutiny by regulators. A close confidante of Greenberg, who

essentially hand-picked Sullivan as his replacement, he also serves as a director in C.V. Starr and SICO. Sullivan has not been accused of any wrongdoing, but regulators are looking for signs that he knew of or oversaw the dubious transactions. Any hint of that and he, too, could be forced out.

Is Greenberg Out of the Picture?

The 79-year-old insurance legend is due to appear before Spitzer for a deposition on April 12 and may face continued scrutiny for his actions, sources say. But Greenberg still retains significant control of AIG through his 1.7 percent personal shareholding and stakes in the private entities that together own another 15.7 percent. Although the full extent of his influence is unknown, Greenberg controls 8.3 percent of SICO's voting stock, is president and CEO of C.V. Starr, where he owns 16.4 percent of the common stock, and is chairman of the Starr Foundation. The structure of SICO, in particular, has also given Greenberg enormous control because anyone who left the company—or was fired—prior to retirement often forfeited lucrative payments. "It was like joining some elite brotherhood where, if you toed the line, you were set for life," says one insider. Investigators and directors may be hard-pressed to force Greenberg out of a private company, and he could continue to exert influence from the background.

Where Was the Board Through This Mess?

For years, AIG had a board that was notoriously clubby and close to Greenberg. Says Patrick McGurn of Institutional Shareholder Services:

"Was there a reform Hank ever put in place that he liked?" But, thanks to shareholder pressure and new governance regulations, the board has become more independent in recent years. More important, perhaps, the investigations have made directors nervous about their own liability—and determined to take proactive action to distance themselves from any scandal, insiders say. They even demanded Greenberg's resignation—an unthinkable act just months ago.

How Do Regulators or Other Critics Propose to Fix These Conflicts of Interest?

One answer is to disband the entities, ban business dealings with the public company, or force AIG executives to end any direct roles in those companies. While a source familiar with the federal probe says regulators haven't yet demanded any specific action, he notes that "none of this is stuff I've seen in other walks of life."

Is AIG Doomed?

Sources close to the investigation are quick to point out that this is no "Enron situation, [although] there were a lot of shenanigans going on. "The insurer sells real products and produces real earnings. The main allegation is that managers went to extreme lengths to smooth those earnings and boost the stock price. Strip out those machinations, and AIG may turn out to be a typical insurer, with big earnings swings up and down, rather than the superior underwriter it appeared to be.

But AIG remains a powerhouse in the industry. It has a diverse mix of industry-leading insurance and financial-services businesses. Moreover, it's a global force with a particularly strong foothold in fast-growing Asian markets, especially China.

Transforming a culture as secretive and ingrained as the one that Greenberg built over four decades would be a monumental task for any CEO—and perhaps an impossible one for a leader who forged his entire career there, as Sullivan did. Moreover, the extent of the com-

pany's liability is unknown. There may be huge fines; there could even be more serious charges. Investors can only guess how much that will batter AIG from here.

Questions

1. Which alleged activities at AIG are potentially questionable on ethical grounds?
2. Why are they questionable?
3. How might different stakeholder groups be affected by these activities?
4. How might a culture of secrecy lead to unethical behavior and why is transparency so important for ensuring ethical conduct?

Source: D. Brady and M. Vickers, "AIG: What Went Wrong." Reprinted from the April 11, 2005, issue of *BusinessWeek* by special permission. Copyright © by the McGraw-Hill Companies, Inc.

BusinessWeek Case in the News

Maria Velazquez was born in a dingy hospital on the U.S.-Mexican border and has been straddling the two nations ever since. The 36-year-old daughter of a bracero, a Mexican migrant who tended California strawberry and lettuce fields in the 1960s, she spent her first nine years like a nomad, crossing the border with her family each summer to follow her father to work. Then her parents

and their six children settled down in a Chicago barrio, where Maria learned English in the local public school and met Carlos Velazquez, who had immigrated from Mexico as a teenager. The two married in 1984, when Maria was 17, and relocated to nearby Cicero, Ill. Her parents returned to their homeland the next year with five younger kids.

The Velazquezes speak fluent English and cherish their middle-

class foothold in America. Maria and Carlos each earn about \$20,000 a year as a school administrator and a graveyard foreman, respectively, and they own a simple three-bedroom home. But they remain wedded to their native language and culture. Spanish is the language at home, even for their five boys ages 6 to 18. The kids speak to each other and their friends in English flecked with "dude" and "man," but

Hispanic Nation

in Cicero, where 77 percent of the 86,000 residents are Hispanic, Spanish dominates.

The older boys snack at local *taquerias* when they don't eat at home, where Maria's cooking runs to dishes like chicken mole and enchiladas. The family reads and watches TV in Spanish and English. The eldest, Jesse, is a freshman at nearby Morton College and dreams of becoming a state trooper; his girlfriend is also Mexican-American. "It's important that they know where they're from, that they're connected to their roots," says Maria, who bounced between Spanish and English while speaking to *BusinessWeek*. She tries to take the kids to visit her parents in the tiny Mexican town of Valle de Guadalupe at least once a year. "It gives them a good base to start from."

The Velazquezes, with their mixed cultural loyalties, are at the center of America's new demographic bulge. Baby boomers, move over—the *bebé* boomers are coming. They are 30 million strong, including some 8 million illegal immigrants—bilingual, bicultural, mostly younger Hispanics who will drive growth in the U.S. population and workforce as far out as statisticians can project. Coming from across Latin America, but predominantly Mexico, and with high birth rates, these immigrants are creating what experts are calling a "tamale in the snake," a huge cohort of kindergarten to thirtysomething Hispanics created by the sheer velocity of their population growth—3 percent a year, versus 0.8 percent for everyone else.

It's not just that Latinos, as many prefer to be called, officially passed African-Americans last year to become the nation's largest minority. Their numbers are so great that, like the post-war baby boomers before them, the Latino Generation is

becoming a driving force in the economy, politics, and culture.

Cultural Clout

It amounts to no less than a shift in the nation's center of gravity. Hispanics made up half of all new workers in the past decade, a trend that will lift them from roughly 12 percent of the workforce today to nearly 25 percent two generations from now. Despite low family incomes, which at \$33,000 a year lag the national average of \$42,000, Hispanics' soaring buying power increasingly influences the food Americans eat, the clothes they buy, and the cars they drive. Companies are scrambling to re-vamp products and marketing to reach the fastest-growing consumer group. Latino flavors are seeping into mainstream culture, too. With Hispanic youth a majority of the under-18 set, or close to it, in cities such as Los Angeles, Miami, and San Antonio, what's hip there is spreading into suburbia, much the way rap exploded out of black neighborhoods in the late 1980s. . . .

The U.S. has never faced demographic change quite like this before. Certainly, the Latino boom brings a welcome charge to the economy at a time when others' population growth has slowed to a crawl. Without a steady supply of new workers and consumers, a graying U.S. might see a long-term slowdown along the lines of aging Japan, says former Housing and Urban Development chief Henry Cisneros, who now builds homes in Hispanic-rich markets such as San Antonio. "Here we have this younger, hard-working Latino population whose best working years are still ahead," he says.

Already, Latinos are a key catalyst of economic growth. Their

disposable income has jumped 29 percent since 2001, to \$652 billion last year, double the pace of the rest of the population according to the Selig Center for Economic Growth at the University of Georgia. Similarly, the ranks of Latino entrepreneurs have jumped by 30 percent since 1998, calculates the Internal Revenue Service. "The impact of Hispanics is huge, especially since they're the fastest-growing demographic," says Merrill Lynch & Co. vice-president Carlos Vaquero, himself a Mexican immigrant based in Houston. Vaquero oversees part of the company's 350-person Hispanic unit, which is hiring 100 mostly bilingual financial advisers this year and which generated \$1 billion worth of new business nationwide last year, double its goal.

Yet the rise of a minority group this distinct requires major adjustments, as well. Already, Hispanics are spurring U.S. institutions to accommodate a second linguistic group. The Labor Department and Social Security Administration are hiring more Spanish-language administrators to cope with the surge in Spanish speakers in the workforce. Politicians, too, increasingly reach out to Hispanics in their own language.

What's not yet clear is whether Hispanic social cohesion will be so strong as to actually challenge the idea of the American melting pot. At the extreme, ardent assimilationists worry that the spread of Spanish eventually could prompt Congress to recognize it as an official second language, much as French is in Canada today. Some even predict a Quebec-style Latino dominance in states such as Texas and California that will encourage separatism, a view expressed in a recent book called *Mexifornia: A State of Becoming* by Victor Davis Hanson, a

history professor at California State University at Fresno. These views have recently been echoed by Harvard University political scientist Samuel P. Huntington in a forthcoming book, *Who Are We*.

These critics argue that legions of poorly educated non-English speakers undermine the U.S. economy. Although the steady influx of low-skilled workers helps keep America's gardens tended and floors cleaned, those workers also exert downward pressure on wages across the lower end of the pay structure. Already, this is causing friction with African Americans, who see their jobs and pay being hit. "How are we going to compete in a global market when 50 percent of our fastest-growing group doesn't graduate from high school?" demands former Colorado Governor Richard D. Lamm, who now co-directs a public policy center at the University of Denver.

Still, many experts think it's more likely that the U.S. will find a new model, more salad bowl than melting pot, that accommodates a Latino subgroup without major upheaval. "America has to learn to live with diversity—the change in population, in [Spanish-language] media, in immigration," says Andrew Erlich, the founder of Erlich Transcultural Consultants Inc. in North Hollywood, Calif. Hispanics aren't so much assimilating as acculturating—acquiring a new culture while retaining their original one—says Felipe Korzenny, a professor of Hispanic marketing at Florida State University.

It boils down to this: How much will Hispanics change America, and how much will America change them? Throughout the country's history, successive waves of immigrants eventually surrendered their native languages and cultures and melted into the middle class. It didn't always happen right away.

During the great European migrations of the 1800s, Germans settled in an area stretching from Pennsylvania to Minnesota. They had their own schools, newspapers, and businesses, and spoke German, says Demetrios G. Papademetriou, co-founder of the Migration Policy Institute in Washington. But in a few generations, their kids spoke only English and embraced American aspirations and habits.

Hispanics may be different, and not just because many are non-whites. True, Maria Velazquez worries that her boys may lose their Spanish and urges them to speak it more. Even so, Hispanics today may have more choice than other immigrant groups to remain within their culture. With national TV networks such as Univision Communications Inc. and hundreds of mostly Spanish-speaking enclaves like Cicero, Hispanics may find it practical to remain bilingual. Today, 78 percent of U.S. Latinos speak Spanish, even if they also know English, according to the Census Bureau.

Back and Forth

The 21 million Mexicans among them also have something else no other immigrant group has had: They're a car ride away from their home country. Many routinely journey back and forth, allowing them to maintain ties that Europeans never could. The dual identities are reinforced by the constant influx of new Latino immigrants—roughly 400,000 a year, the highest flow in U.S. history. The steady stream of newcomers will likely keep the foreign-born, who typically speak mostly or only Spanish, at one-third of the U.S. Hispanic population for several decades. Their presence means that "Spanish is constantly refreshed, which is one of the key contrasts with what people think of

as the melting pot," says Roberto Suro, director of the Pew Hispanic Center, a Latino research group in Washington.

A slow pace of assimilation is likely to hurt Hispanics themselves the most, especially poor immigrants who show up with no English and few skills. Latinos have long lagged in U.S. schools, in part because many families remain cloistered in Spanish-speaking neighborhoods. Their strong work ethics can compound the problem by propelling many young Latinos into the workforce before they finish high school. So while the Hispanic high-school-graduation rate has climbed 12 percentage points since 1980, to 57 percent, that's still woefully short of the 88 percent for non-Hispanic whites and 80 percent for African-Americans.

Meld into the Mainstream

The failure to develop skills leaves many Hispanics trapped in low-wage service jobs that offer few avenues for advancement. Incomes may not catch up anytime soon, either, certainly not for the millions of undocumented Hispanics. Most of these, from Mexican street-corner day laborers in Los Angeles to Guatemalan poultry-plant workers in North Carolina, toil in the underbelly of the U.S. economy. Many low-wage Hispanics would fare better economically if they moved out of the barrios and assimilated into U.S. society. Most probably face less racism than African-Americans, since Latinos are a diverse ethnic and linguistic group comprising every nationality from Argentinians, who have a strong European heritage, to Dominicans, with their large black population. Even so, the pull of a common language may keep many in a country apart.

Certainly immigrants often head for a place where they can get support from fellow citizens, or even former neighbors. Some 90 percent of immigrants from Tonatico, a small town 100 miles south of Mexico City, head for Waukegan, Ill., joining 5,000 Tonaticans already there. In Miami, of course, Cubans dominate. "Miami has Hispanic banks, Hispanic law firms, Hispanic hospitals, so you can more or less conduct your entire life in Spanish here," says Leopoldo E. Guzman, 57. He came to the U.S. from Cuba at 15 and turned a Columbia University degree into a job at Lazard Frères & Co. before founding investment bank Guzman & Co. . . .

It's still possible that Cicero's Latino children will follow the path of so many other immigrants and move out into non-Hispanic neighborhoods. If they do, they, or at least their children, will likely all but abandon Spanish, gradually marry non-Hispanics, and meld into the mainstream.

But many researchers and academics say that's not likely for many Hispanics. In fact, a study of assimilation and other factors shows that while the number of Hispanics who prefer to speak mostly Spanish has dipped in recent years as the children of immigrants grow up with English, there has been no increase in those who prefer only English. Instead, the HispanTelligence study found that the group speaking both languages has climbed six percentage points since 1995, to 63 percent, and is likely to jump to 67 percent in 2010.

The trend to acculturate rather than assimilate is even more stark among Latino youth. Today, 97 percent of Mexican kids whose parents are immigrants and 76 percent of other Hispanic immigrant children know Spanish, even as nearly

90 percent also speak English very well, according to a decade-long study by University of California at Irvine sociologist Rubén G. Rumbaut. More striking, those Latino kids keep their native language at four times the rate of Filipino, Vietnamese, or Chinese children of immigrants. "Before, immigrants tried to become Americans as soon as possible," says Sergio Bendixen, founder of Bendixen & Associates, a polling firm in Coral Gables, Fla., that specializes in Hispanics. "Now, it's the opposite."

Selling in Spanish

In its eagerness to tap the exploding Hispanic market, Corporate America itself is helping to reinforce Hispanics' bicultural preferences. Last year, Procter & Gamble Co. spent \$90 million on advertising directed at Latinos for 12 products such as Crest and Tide—10 percent of its ad budget for those brands and a 28 percent hike in just a year. Sure, P&G has been marketing to Hispanics for decades, but spending took off after 2000, when the company set up a 65-person bilingual team to target Hispanics. Now, P&G tailors everything from detergent to toothpaste to Latino tastes. Last year, it added a third scent to Gain detergent called "white-water fresh" after finding that 57 percent of Hispanics like to smell their purchases. Now, Gain's sales growth is double-digit in the Hispanic market, outpacing general U.S. sales. "Hispanics are a cornerstone of our growth in North America," says Graciela Eleta, vice-president of P&G's multicultural team in Puerto Rico.

Other companies are making similar assumptions. In 2002, Cypress (Calif.)-based PacifiCare Health Systems Inc. hired Russell A. Bennett, a longtime Mexico City

resident, to help target Hispanics. He soon found that they were already 20 percent of PacifiCare's 3 million policyholders. So Bennett's new unit, Latino Health Solutions, began marketing health insurance in Spanish, directing Hispanics to Spanish-speaking doctors, and translating documents into Spanish for Hispanic workers. "We knew we had to remake the entire company, linguistically and culturally, to deal with this market," says Bennett.

A few companies are even going all-Spanish. After local Hispanic merchants stole much of its business in a Houston neighborhood that became 85 percent Latino, Kroger Co., the nation's No. 1 grocery chain, spent \$1.8 million last year to convert the 59,000-sq.ft. store into an all-Hispanic *supermercado*. Now, Spanish-language signs welcome customers, and catfish and banana leaves line the aisles. Across the country, Kroger has expanded its private-label Buena Comida line from the standard rice and beans to 105 different items.

As the ranks of Spanish speakers swell, Spanish-language media are transforming from a niche market into a stand-alone industry. Ad revenues on Spanish-language TV should climb by 16 percent this year, more than other media segments, according to TNS Media Intelligence/CMR. The audience of Univision, the No. 1 Spanish-language media conglomerate in the U.S., has soared by 44 percent since 2001, and by 146 percent in the 18- to 34-year-old group. Many viewers have come from English-language networks, whose audiences have declined in that period.

In fact, Univision tried to reach out to assimilated Hispanics a few years ago by putting English-language programs on its cable channel Galavision. They bombed,

says Univision President Ray Rodriguez, so he switched back to Spanish-only in 2002—and 18- to 34-year-old viewership shot up by 95 percent that year. “We do what the networks don’t, and that’s devote a lot of our show to what interests the Latino community,” says Univision news anchor Jorge Ramos. . . .

For more than 200 years, the nation has succeeded in weaving the foreign-born into the fabric of U.S. society, incorporating strands of new cultures along the way. With their huge numbers, Hispanics are adding all kinds of new influences. Cinco de Mayo has joined St. Patrick’s Day as a public celebration in some neighborhoods,

and burritos are everyday fare. More and more, Americans hablan Español. Will Hispanics be absorbed just as other waves of immigrants were? It’s possible, but more likely they will continue to straddle two worlds, figuring out ways to remain Hispanic even as they become Americans.

Questions

1. What are the implications of the influx of Hispanics for diversity in the United States?
2. What are the costs and benefits for Hispanics of trying to retain their own cultures while assimilating into the U.S. culture?

3. Is the notion of the United States as a “melting pot” outdated? Why or why not?
4. To what extent does increasing globalization mean more multiculturalism and more multilingual citizens in a variety of countries, including the United States?

Source: Excerpted from Brian Grow, “Hispanic Nation.” Reprinted from the March 15, 2004, issue of *BusinessWeek* by special permission. Copyright © 2004 by the McGraw-Hill Companies.

CHAPTER

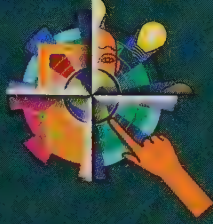
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Managing in the Global Environment

Learning Objectives

After studying this chapter, you should be able to:

- Explain why the ability to perceive, interpret, and respond appropriately to the organizational environment is crucial for managerial success.
- Identify the main forces in a global organization's task and general environments, and describe the challenges that each force presents to managers.
- Explain why the global environment is becoming more open and competitive and why barriers to the global transfer of goods and services are falling, increasing the opportunities, complexities, challenges, and threats that managers face.



Management Snapshot

Korea's LG (Lucky Goldstar) Wants to Be the New Leader in Global Electronics

Why is managing in a global environment so complex today?

Competition in the global marketplace is fierce. Nowhere is this more true than in the electronics industry, where in the 1970s Japanese companies, by virtue of their ability to make high-quality, low-cost stereos and televisions, drove almost all large U.S. and European electronics companies out of the market, with the exception of Phillips. By the 1990s, however, Japanese companies came under threat themselves from even lower-cost Asian competitors like Korea's Samsung. Samsung at first copied the high-quality technology of Japanese companies and then made and sold stereos and TVs at much lower cost. However, in the mid-1990s Samsung began a major push to become a technological leader itself, focusing on making high-quality components such as flash memory and flat screen displays, and then improving upon the technology of its Japanese competitors.

By the 2000s Samsung became the second most profitable technology company in the world after Microsoft. In the meantime, global technology leader Sony had been suffering

badly because of high operating costs and because its high-priced products made the company uncompetitive. Moreover, Sony had missed major new developments in the market, such as the growing popularity of digital music



LG CEO Ssang-Su Kim, right, and President Woo Hyun Paik, look through 3-D glasses while viewing a display at the company's booth at the 2005 Consumer Electronics Show in Las Vegas.

players. Here, Apple's iPod was the market leader but in 2005 Asian electronics companies were rushing to bring out sleek, powerful, and much less expensive iPod clones.

As competition in the digital music player market suggests, the pace of global competition is not slackening. And, in Korea there is a company named LG, formerly called Lucky Goldstar, that wants to beat its national rival,

Samsung, at its own game. LG wants its engineers to imitate all Samsung's technological advances and then to outperform it, just as Samsung recently outperformed companies like Sony and Hitachi.

To make this new strategy work, LG's CEO, Kim Ssang Su, has instructed all his top managers to reduce costs by 25 percent while working to innovate new products that will make LG a "top notch player with great people and great global ambitions." In the last two years Kim has energized LG toward this goal. He has formed a strategic alliance with Phillips, making them the second largest supplier of flat screen TVs in the world. Kim has also made

the company a leader in other fast-growing markets. For instance, LG is currently the biggest global supplier of air conditioners. In the important cell phone market, in partnership with Verizon, LG is threatening the dominance of Nokia and Samsung in these markets too.¹

In today's global marketplace competition is fast changing and intense; managers must constantly strive to maintain and build their companies' competitive advantage or like the electronic companies of the 1980s they will disappear. More agile and motivated companies like LG will always emerge to compete with leaders like Samsung and Sony to replace them at the top rung of the global ladder.

Overview

global organization

An organization that operates and competes in more than one country.

Top managers of global companies like LG, Samsung, and Sony operate in an environment where they are competing with other companies for scarce and valuable resources. Managers of companies large and small have concluded that in order to survive in the 21st century most organizations must become **global organizations**, organizations that operate and compete not only domestically, at home, but also globally, in countries around the world. Operating in a global environment is uncertain and unpredictable because it is complex and constantly changing, as is the electronics industry.

If organizations are to adapt to this changing environment, their managers must learn to understand the forces that operate in it and how these forces give rise to opportunities and threats. In this chapter, we examine why the environment, both domestically and globally, has become more open, vibrant, and competitive. We examine how forces in the task and general environments affect global organizations and their managers. By the end of this chapter, you will appreciate the changes that have been taking place in the environment and understand why it is important for managers to develop a global perspective as they strive to increase organizational efficiency and effectiveness.

What Is the Organizational Environment?

organizational environment

The set of forces and conditions that operate beyond an organization's boundaries but affect a manager's ability to acquire and utilize resources.

The **organizational environment** is a set of forces and conditions outside the organization's boundaries that have the potential to affect the way the organization operates.² These forces change over time and thus present managers with *opportunities* and *threats*. Changes in the environment, such as the introduction of new technology or the opening of global markets, create opportunities for managers to obtain resources or enter new markets and thereby strengthen their organizations. In contrast, the rise of new competitors, a global economic recession, or an oil shortage poses threats that can devastate an organization if managers are unable to obtain resources or sell the organization's goods and services. The quality of managers' understanding of organizational environment forces and their ability to respond appropriately to those forces, such as Kim's plan for LG, are critical factors affecting organizational performance.

task environment

The set of forces and conditions that originate with suppliers, distributors, customers, and competitors and affect an organization's ability to obtain inputs and dispose of its outputs because they influence managers on a daily basis.

general

environment The wide-ranging economic, technological, sociocultural, demographic, political and legal, and global forces that affect an organization and its task environment.

In this chapter we explore the nature of these forces and consider how managers can respond to them. To identify opportunities and threats caused by forces in the organizational environment, it is helpful for managers to distinguish between the *task environment* and the more encompassing *general environment* (see Figure 4.1, page 139).

The **task environment** is the set of forces and conditions that originate with suppliers, distributors, customers, and competitors; these forces and conditions affect an organization's ability to obtain inputs and dispose of its outputs. The task environment contains the forces that have the most *immediate* and *direct* effect on managers because they pressure and influence managers on a daily basis. When managers turn on the radio or television, arrive at their offices in the morning, open their mail, or look at their computer screens, they are likely to learn about problems facing them because of changing conditions in their organization's task environment.

The **general environment** includes the wide-ranging economic, technological, sociocultural, demographic, political and legal, and global forces that affect the organization and its task environment. For the individual manager, opportunities and threats resulting from changes in the general environment are often more difficult to identify and respond to than are events in the task environment. However, changes in these forces can have major impacts on managers and their organizations.

Figure 4.1**Forces in the Organizational Environment**

The Task Environment

Forces in the task environment result from the actions of suppliers, distributors, customers, and competitors (see Figure 4.1). These four groups affect a manager's ability to obtain resources and dispose of outputs on a daily, weekly, and monthly basis and thus have a significant impact on short-term decision making.

Suppliers

suppliers Individuals and organizations that provide an organization with the input resources that it needs to produce goods and services.

Suppliers are the individuals and companies that provide an organization with the input resources (such as raw materials, component parts, or employees) that it needs to produce goods and services. In return, the supplier receives compensation for those goods and services. An important aspect of a manager's job is to ensure a reliable supply of input resources.

Take Dell Computer, for example, the company we focused on in Chapter 1. Dell has many suppliers of component parts such as microprocessors (Intel and AMD) and disk drives (Quantum and Seagate Technologies). It also has suppliers of preinstalled software, including the operating system (Microsoft) and specific applications software (IBM, Oracle, and America Online). Dell's providers of capital, such as banks and financial institutions, are also important suppliers. Cisco Systems and Oracle are important providers of Internet hardware and software for dot-coms.

Dell has several suppliers of labor. One source is the educational institutions that train future Dell employees and therefore provide the company with skilled workers. Another is trade unions, organizations that represent employee interests and can control the supply of labor by exercising the right of unionized workers to strike. Unions also can influence the terms and conditions under which labor is employed. Dell's workers are not unionized; when layoffs became necessary due to an economic slowdown in the early 2000s, Dell had few problems in laying off workers to reduce costs. In organizations and industries where unions are very strong, however, an important part of a manager's job is negotiating and administering agreements with unions and their representatives.

Changes in the nature, numbers, or types of any supplier result in forces that produce opportunities and threats to which managers must respond if their organizations are to prosper. For example, a major supplier-related threat that confronts managers arises when suppliers' bargaining position is so strong that they can raise the prices of the inputs they supply to the organization. A supplier's bargaining position is especially strong when (1) the supplier is the sole source of an input and (2) the input is vital to the organization.³ For example, for 17 years G. D. Searle was the sole supplier of NutraSweet, the artificial sweetener used in most diet soft drinks. Not only was NutraSweet an important ingredient in diet soft drinks, but it also was one for which there was no acceptable substitute (saccharin and other artificial sweeteners raised health concerns). Searle earned its privileged position because it invented and held the patent for NutraSweet. Patents prohibit other organizations from introducing competing products for 17 years. In 1992, Searle's patent expired, and many companies began to produce products similar to NutraSweet. Prior to 1992, Searle was able to demand a high price for NutraSweet, charging twice as much as the price of an equivalent amount of sugar. Paying that price raised the costs of soft-drink manufacturers,

including Coca-Cola and PepsiCo, which had no alternative but to buy the product.⁴ Today, NutraSweet is still the artificial sweetener of choice, but soft-drink companies pay much less for it.

In contrast, when an organization has many suppliers for a particular input, it is in a relatively strong bargaining position with those suppliers and can demand low-cost, high-quality inputs from them. Often, an organization can use its power with suppliers to force them to reduce their prices, as Dell frequently does.

Dell, for example, is constantly searching for global low-cost suppliers to keep its PC prices competitive. At a global level, managers have the opportunity to buy products from foreign suppliers or to become their own suppliers and manufacture their own products abroad. It is important that managers recognize the opportunities and threats associated with managing the global supply chain. On the one hand, gaining access to low-cost products made abroad represents an opportunity for U.S. companies to lower their input costs. On the other hand, managers who fail to utilize low-cost foreign suppliers create a threat and put their organizations at a competitive disadvantage.⁵ Levi Strauss, for example, was slow to realize that it could not compete with the low-priced jeans sold by Wal-Mart and other retailers, and it was eventually forced to close almost all of its U.S. jean factories and utilize low-cost foreign suppliers to keep the price of its jeans competitive. Now it sells its low-priced jeans in Wal-Mart! The downside to global outsourcing is, of course, the loss of millions of U.S. jobs, an issue we have discussed in previous chapters.

A common problem facing managers of large global companies such as Ford, Procter & Gamble, and IBM is managing the development of a global network of suppliers that will allow their companies to keep costs down and quality high. For example, the building of Boeing's newest jet airliner, the 777, required 132,500 engineered parts produced around the world by 545 suppliers.⁶ While Boeing makes the majority of these parts, eight Japanese suppliers make parts for the 777's fuselage, doors, and wings; a Singapore supplier makes the doors for the plane's forward landing gear; and three Italian suppliers manufacture wing flaps. Boeing's rationale for buying so many inputs from foreign suppliers is that these suppliers are the best in the world at performing their particular activity and doing business with them helps Boeing to produce a high-quality final product, a vital requirement given the need for aircraft safety and reliability.⁷

The purchasing activities of global companies have become increasingly complicated as a result of the development of a whole range of skills and competencies in different countries around the world. It is clearly in their interests to search out the lowest-cost, best-quality suppliers no matter where they may be. Also, the Internet makes it possible for companies to coordinate complicated, arm's-length exchanges involving the purchasing of inputs and the disposal of outputs.

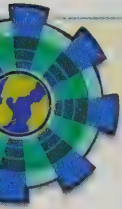
Global outsourcing is the process by which organizations purchase inputs from other companies or produce inputs themselves throughout the world to lower their production costs and improve the quality or design of their products.⁸ To take advantage of national differences in the cost and quality of resources such as labor or raw materials, GM might build its own engines in one country, transmissions in another, and brakes in a third and buy other components from hundreds of global suppliers. Trade expert Robert Reich once calculated that of the \$20,000 that customers pay GM for a Pontiac Le Mans, about \$6,000 goes to South Korea, where the Le Mans is assembled; \$3,500, to Japan for advanced components such as engines, transaxles, and electronics; \$1,500, to Germany, where the Le Mans was designed; \$800, to Taiwan, Singapore, and Japan for small components; \$500,

global outsourcing

The purchase of inputs from foreign suppliers or the production of inputs abroad to lower production costs and to improve product quality or design.

to Britain for advertising and marketing services; and about \$100, to Ireland for data-processing services. The remaining \$7,000 goes to GM—and to the lawyers, bankers, and insurance agents that GM retains in the United States.⁹

Is the Le Mans a U.S. product? Yes, but it is also a Korean product, a Japanese product, and a German product. Today, such global exchanges are becoming so complex that specialized organizations are emerging to help manage global organizations' supply chains, that is, the flow of inputs necessary to produce a product. One example is Li & Fung, profiled below in "Managing Globally."



Managing Globally

Global Supply Chain Management

Finding the foreign suppliers that offer the lowest-priced and highest-quality products is an important task facing the managers of global organizations. Since these suppliers are located in thousands of cities in many countries around the world, finding them is a difficult business. Often, global companies use the services of foreign intermediaries or brokers, located near these suppliers, to find the one that best meets their input requirements. Li & Fung, now run by brothers Victor and William Fung, is one of the brokers that has helped hundreds of global companies to locate suitable foreign suppliers, especially suppliers in mainland China.¹⁰

In the 2000s, however, managing global companies' supply chains became a more complicated task. To reduce costs, foreign suppliers were increasingly *specializing* in just one part of the task of producing a product. For example, in the past, a company such as Target might have negotiated with a foreign supplier to manufacture 1 million units of some particular shirt at a certain cost per unit. But with specialization, Target might find it can reduce the costs of producing the shirt even further by splitting apart the operations involved in its production and having *different* foreign suppliers, often in *different* countries, perform each operation. For example, to get the lowest cost per unit, rather than negotiating with a single foreign supplier over the price of making a particular shirt, Target might

first negotiate with a yarn manufacturer in Vietnam to make the yarn; then ship the yarn to a Chinese supplier to weave it into cloth; and then ship the cloth to several different factories in Malaysia and the Philippines to cut the fabric and sew the shirts. Then, another foreign company might take responsibility for packaging and shipping the shirts to wherever in the world they are required. Because a company such as Target has thousands of different clothing products under production, and they change all the time, the problems of managing such a supply chain to get the full cost savings from global expansion are clearly difficult and costly.

Li & Fung capitalized on this opportunity. Realizing that many global companies do not have the time or expertise to find such specialized low-price suppliers, its founders moved quickly to provide



Clothing companies like Target keep their prices low by locating in countries abroad where labor costs are low.

such a service. Li & Fung employs 3,600 agents who travel across 37 countries to locate new suppliers and inspect existing suppliers to find new ways to help its global clients get lower prices or higher-quality products. Global companies are happy to outsource their supply chain management to Li & Fung because they realize significant cost savings. Even though they pay a hefty fee to Li & Fung, they avoid the costs of employing their own agents. As the complexity of supply chain management continues to increase, more and more companies like Li & Fung are appearing.

Distributors

Distributors

Organizations that help other organizations sell their goods or services to customers.

Distributors are organizations that help other organizations sell their goods or services to customers. The decisions that managers make about how to distribute products to customers can have important effects on organizational performance. For example, package delivery companies such as Federal Express, UPS, and the U.S. Postal Service became vital distributors for the millions of items bought online and shipped to customers by dot-com companies.

The changing nature of distributors and distribution methods can bring opportunities and threats for managers. If distributors become so large and powerful that they can control customers' access to a particular organization's goods and services, they can threaten the organization by demanding that it reduce the prices of its goods and services.¹¹ For example, the huge retail distributor Wal-Mart controls its suppliers' access to a great number of customers and thus often demands that its suppliers reduce their prices. If an organization such as Procter & Gamble refuses to reduce its prices, Wal-Mart might respond by buying products only from Procter & Gamble's competitors—companies such as Unilever and Dial. In 2004, Wal-Mart announced that by 2006 all its suppliers must adopt a new wireless scanning technology that will reduce its cost of distributing products to its stores or it will stop doing business with them.¹²

In contrast, the power of a distributor may be weakened if there are many options. This has been the experience of the three broadcast television networks—ABC, NBC, and CBS. Their ability to demand lower prices from the producers of television programs has been weakened. The presence of hundreds of new cable television channels has reduced the three networks' clout by decreasing their share of the viewing audience to less than 40 percent in 2004, down from more than 90 percent a decade ago. Similarly, because there are many package delivery companies, the dot-coms would not really be threatened if one delivery firm tried to increase its prices; they could simply switch delivery companies.

Another force that creates opportunities and threats for global managers is the nature of a country's distribution system. For example, consider how Japan's systems of distributing Japanese-made products caused problems for Toys 'R' Us managers when they were seeking to establish a chain of stores in Japan. Traditionally, Japanese manufacturers sold their products only by means of wholesalers with which they had developed long-term business relationships. Because the wholesalers added their own price markup, the price Toys 'R' Us had to pay for Japanese toys increased, and this thwarted the U.S. company's attempt to establish a competitive advantage in Japan based on price discounting. To keep its costs low, Toys 'R' Us insisted on buying directly from Japanese manufacturers, but the manufacturers refused.

This standoff was finally broken by Japan's deep recession in the early 1990s. Faced with slumping orders, computer-game maker Nintendo reversed its earlier decision and agreed to sell merchandise directly to Toys 'R' Us. Soon a host of other Japanese toy companies followed Nintendo's lead. With these major problems solved, average sales in Toys 'R' Us's Japanese stores were between \$15 million and \$20 million a year, roughly double the sales per store in the United States. As Toys 'R' Us discovered in Japan, the traditional means by which goods and services are distributed and sold to customers can present challenges to managers of organizations pursuing international expansion. Managers must identify the hidden problems surrounding the distribution and sale of goods and services—such as anticompetitive government regulations, discussed later—in order to discover hidden threats early and find ways to overcome them before significant resources are invested.

Customers

customers

Individuals and groups that buy the goods and services that an organization produces.

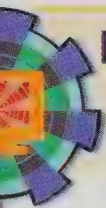
Customers are the individuals and groups that buy the goods and services that an organization produces. For example, Dell's customers can be segmented into several distinct groups: (1) individuals who purchase PCs for home use, (2) small companies, (3) large companies, (4) government agencies, and (5) educational institutions. Changes in the number and types of customers or changes in customers' tastes and needs result in opportunities and threats. An organization's success depends on its response to customers. In the PC industry, customers are demanding lower prices and increased multimedia capability, and PC companies must respond to the changing types and needs of customers.¹³ A school, too, must adapt to the changing needs of its customers. For example, if more Spanish-speaking students enroll, additional classes in English as a second language may need to be scheduled. A manager's ability to identify an organization's main customers and produce the goods and services they want is a crucial factor affecting organizational and managerial success.

The most obvious opportunity associated with expanding into the global environment is the prospect of selling goods and services to new customers, as Amazon.com's CEO Jeff Bezos discovered when he began to start operating in many countries abroad. Similarly, Accenture and Cap Gemini, two large consulting companies, have established operations throughout the world and recruit and train thousands of foreign consultants to serve the needs of customers in a wide variety of countries.

Today, once-distinct national markets are merging into one huge global marketplace where the same basic product can be sold to customers worldwide. This consolidation is occurring both for consumer goods and for business products and has created enormous opportunities for managers. The global acceptance of Coca-Cola, Sony Walkmans, McDonald's hamburgers, Doc Martin boots, and Nokia cell phones is a sign that the tastes and preferences of consumers in different countries are beginning to become more similar.¹⁴ Likewise, large global markets currently exist for business products such as telecommunications equipment, electronic components, computer services, and financial services. Thus, Motorola sells its telecommunications equipment, Intel its microprocessors, and SAP its business systems management software to customers throughout the world.

Nevertheless, despite evidence that the same goods and services are receiving acceptance from customers worldwide, it is important not to place too much

emphasis on this development. Because national cultures differ in many ways, significant differences between countries in consumer tastes and preferences still remain. These differences often require that managers customize goods and services to suit the preferences of local consumers. For example, despite McDonald's position as a leading global organization, its management has recognized a need for local customization. In Brazil, McDonald's sells a soft drink made from the guarana, an exotic berry that grows along the Amazon River. In Malaysia, McDonald's sells milk shakes flavored with durian, a strong-smelling fruit that local people consider an aphrodisiac.¹⁵ Similarly, when Mattel decided to begin selling Barbie dolls in Japan, it had to redesign the doll's appearance (color of hair, facial features, and so on) to suit the tastes of its prospective customers. Companies also have to be careful to design and select the right kind of information systems and Web sites to enable customers to buy their products.



Information Technology Byte

Designing Global Information Systems

As more and more customers buy products online, the importance of a company's Web site is increasing. Good design is essential for attracting not only domestic customers but also those overseas. Domestically, the problems involved in designing a good Web site caused even information technology expert Wal-Mart to close down its Web site for two weeks in 2000 while it reworked its search and ordering system.¹⁶ Dell Computer, however, has one of the easiest-to-use and most popular Web sites of a U.S. company, so imagine its surprise when, after creating a Japanese Web site, it found that Japanese customers were not attracted to it at all.

The reason? Dell's designers decided to give the Web site a thick black border around the outside of the screen, and in Japan black is a symbol of negative feelings and emotions.¹⁷ Dell's designers moved quickly to solve this problem, and now, whenever they create a Web site in a foreign country, they are careful to work with local managers to make sure that their screen colors or icons do not offend local tastes or customs. Another common problem is linguistic errors. To avoid embarrassing mistakes, companies must ensure that designers are correctly using the country's language. This is particularly important in Asia, where local scripts are easy to misinterpret. Also, companies must take into consideration how customers like to pay for their online products. Unlike U.S. consumers, who make constant use of credit cards, consumers in Germany and Japan like to avoid debt and pay by cash or debit card.

To respond to these problems, companies such as Yahoo, Dell, and SAP are increasingly developing local management teams based in each country in which they operate to oversee their businesses.¹⁸ Often, this can involve giving domestic managers foreign assignments to help develop their global expertise. For example, managers can learn about each country's different regulatory environment; they can also help develop a strategy to customize products to suit local tastes. In this way, a company's global knowledge increases.

Beyond having Web sites directed at customers, companies also have to be sure they are developing information systems and intranets that are understandable and usable not only by domestic and foreign managers but also by their

suppliers worldwide. For example, Wal-Mart's push to become a global company has led it to develop a global knowledge management system that tells foreign suppliers what kinds of products Wal-Mart requires and what it is willing to pay for them.¹⁹ Foreign suppliers can then bid for Wal-Mart's business; in this way, Wal-Mart makes sure it is securing the lowest prices. Its global knowledge system is also used to share merchandising information from country to country so that Wal-Mart can quickly take advantage of changing trends and ideas.

Competitors

competitors

Organizations that produce goods and services that are similar to a particular organization's goods and services.

One of the most important forces that an organization confronts in its task environment is competitors. **Competitors** are organizations that produce goods and services similar to a particular organization's goods and services. In other words, competitors are organizations vying for the same customers. Dell's competitors include other domestic manufacturers of PCs (such as Apple, Compaq, and Gateway) as well as foreign competitors (such as Sony and Toshiba in Japan and Group Bull in France). Dot-com stockbroker E*Trade has other dot-com competitors, like Ameritrade and TD Waterhouse, as well as bricks-and-clicks competitors, such as Merrill Lynch and Charles Schwab.

Rivalry between competitors is potentially the most threatening force that managers must deal with. A high level of rivalry often results in price competition, and falling prices reduce access to resources and lower profits. In the 2000s, competition in the personal computer industry became intense not only because of an economic slowdown but also because Dell was aggressively cutting costs and prices to try to increase its market share. Michael Dell announced that he wanted to increase Dell's market share from 13 to 40 percent—and Dell was already the global leader.²⁰ By 2004 Dell had increased its global market share to 35 percent.²¹ Unable to compete, IBM announced it was exiting the PC business because it was losing millions in its battle against low-cost rivals such as Dell and Gateway.

potential competitors

Organizations that presently are not in a task environment but could enter if they so choose.

Although the rivalry between existing competitors is a major threat, so is the potential for new competitors to enter the task environment. **Potential competitors** are organizations that are not presently in a task environment but could enter if they so choose. Amazon.com, for example, is not currently in the retail furniture or appliance business, but it could enter these businesses if its managers decided it could profitably sell such products. When new competitors enter an industry, competition increases and prices decrease.

barriers to entry

Factors that make it difficult and costly for an organization to enter a particular task environment or industry.

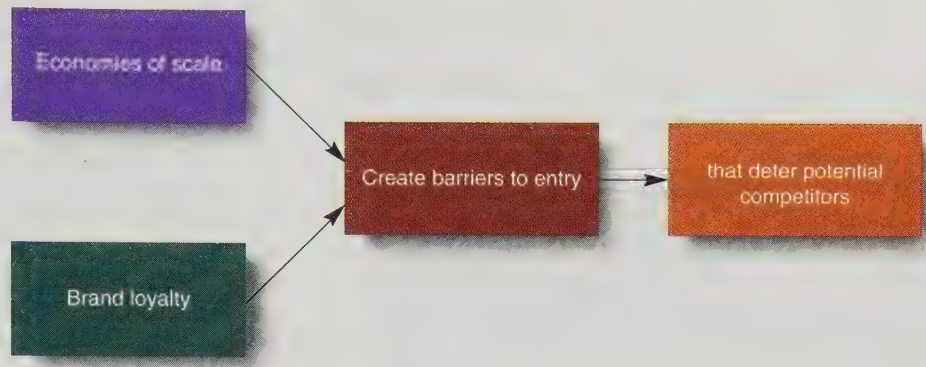
In general, the potential for new competitors to enter a task environment (and thus boost the level of competition) is a function of barriers to entry.²² **Barriers to entry** are factors that make it difficult and costly for an organization to enter a particular task environment or industry.²³ In other words, the more difficult and costly it is to enter the task environment, the higher are the barriers to entry. The higher the barriers to entry, the fewer the competitors in an organization's task environment and thus the lower the threat of competition. With fewer competitors, it is easier to obtain customers and keep prices high.

economies of scale

Cost advantages associated with large operations.

Barriers to entry result from three main sources: economies of scale, brand loyalty, and government regulations that impede entry (see Figure 4.2). **Economies of scale** are the cost advantages associated with large operations. Economies of scale result from factors such as manufacturing products in very large quantities, buying inputs in bulk, or making more effective use of organizational resources than do

Figure 4.2
Barriers to Entry and Competition



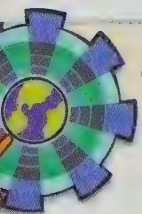
competitors by fully utilizing employees' skills and knowledge. If organizations already in the task environment are large and enjoy significant economies of scale, then their costs are lower than the costs of potential entrants will be, and newcomers will find it very expensive to enter the industry. Amazon.com, for example, enjoys significant economies of scale relative to most other dot-com companies.²⁴

brand loyalty
Customers' preference for the products of organizations currently existing in the task environment.

Brand loyalty is customers' preference for the products of organizations currently existing in the task environment. If established organizations enjoy significant brand loyalty, then a new entrant will find it extremely difficult and costly to obtain a share of the market. Newcomers must bear huge advertising costs to build customer awareness of the goods or services they intend to provide.²⁵ Both Amazon.com and Yahoo, for example, two of the first dot-coms to go online, enjoy a high level of brand loyalty and have some of the highest Web-site hit rates of all dot-coms (the latter also allows them to increase their advertising revenues).

In some cases, *government regulations* function as a barrier to entry at both the industry and the country levels. Many industries that were deregulated, such as air transport, trucking, utilities, and telecommunications, experienced a high level of new entry after deregulation; this forced existing companies in those industries to operate more efficiently or risk being put out of business.

At the national and global level, administrative barriers are government policies that create a barrier to entry and limit imports of goods by foreign companies. Japan is well known for the many ways in which it attempts to restrict the entry of foreign competitors or lessen their impact on Japanese firms. For example, why do Dutch companies export tulip bulbs to almost every country in the world except Japan? Japanese customs inspectors insist on checking every tulip bulb by cutting the stems vertically down the middle, and even Japanese ingenuity cannot put them back together.²⁶ Japan has come under intense pressure to relax and abolish such regulations, as the following suggests.



Managing Globally

American Rice Invades Japan

The Japanese rice market, similar to many other Japanese markets, was closed to foreign competitors until 1993 to protect Japan's thousands of high-cost, low-output rice farmers. Rice cultivation is expensive in Japan because of the country's mountainous terrain, so Japanese consumers have always paid high prices for rice. Under foreign pressure, the Japanese government opened the market, and foreign competitors are now allowed to export to Japan 8 percent of its

annual rice consumption. Despite the still-present hefty foreign tariff on rice—\$2.33 per 2.2 pounds—U.S. rice sells for \$14 per pound bag while Japanese rice sells for about \$19. With the recession affecting Japan, price-conscious consumers are turning to foreign rice, which has hurt domestic farmers.



A Japanese businessman receives a lunch box at a Nippon restaurant shop at the Tokyo Railway Station. Nippon began selling lunch boxes prepared from U.S. rice, frozen and imported from the United States, in 2001, drawing harsh protests from Japanese rice farmers.

In 2001, however, an alliance between organic rice grower Lundberg Family Farms of California and the Nippon Restaurant Enterprise Co. found a new way to break into the Japanese rice market. Because there is no tariff on rice used in processed foods, Nippon takes the U.S. organic rice and converts it into “O-bento,” an organic hot boxed lunch packed with rice, vegetables, chicken, beef, and salmon, all imported from the United States. The new lunches, which cost about \$4 compared to a Japanese rice bento that costs about \$9, are sold at railway stations and other outlets throughout Japan.²⁷ They are proving to be very popular and are creating a storm of protest from Japanese rice farmers, who already have been forced to leave 37 percent of their rice fields idle and grow less-profitable crops because of the entry of U.S. rice growers. Japanese and foreign companies are increasingly forming alliances to find new ways to break into the high-price Japanese market, and, little by little, Japan’s restrictive trade practices are being whittled away.

In summary, intense rivalry among competitors creates a task environment that is highly threatening and causes difficulty for managers trying to gain access to the resources an organization needs. Conversely, low rivalry results in a task environment where competitive pressures are more moderate and managers have greater opportunities to acquire the resources they need for their organizations to be effective.

The General Environment

Economic, technological, sociocultural, demographic, political and legal, and global forces in an organization’s general environment can have profound effects on the organization’s task environment, effects that may not be evident to managers. For example, the sudden, dramatic upheavals in the Internet and dot-com industry environment were brought about by a combination of changing Internet technology, the softening U.S. stock market and economy, and increasing fears about the health of the global economy. These changes triggered intense competition between dot-com companies that further worsened the industry situation.

The implication is clear: Managers must constantly analyze forces in the general environment because these forces affect ongoing decision making and planning. Next, we discuss the major forces in the general environment, and examine their impacts on an organization’s task environment.

Economic forces

economic forces

Interest rates, inflation, unemployment, economic growth, and other factors that affect the general health and well-being of a nation or the regional economy of an organization.

Economic forces affect the general health and well-being of a country or world region. They include interest rates, inflation, unemployment, and economic growth. Economic forces produce many opportunities and threats for managers. Low levels of unemployment and falling interest rates mean a change in the customer base: More people have more money to spend, and as a result organizations have an opportunity to sell more goods and services. Good economic times affect supplies: Resources become easier to acquire, and organizations have an opportunity to flourish, as high-tech companies did throughout the 1990s. The high-techs made record profits as the economy boomed in large part because of advances in information technology and growing global trade.

In contrast, worsening macroeconomic conditions, as in the early 2000s, pose a major threat because they limit managers' ability to gain access to the resources their organizations need. Profit-oriented organizations such as retail stores and hotels have fewer customers for their goods and services during economic downturns. Not-for-profit organizations such as charities and colleges receive fewer donations during economic downturns. Even a moderate deterioration in national or regional economic conditions can seriously affect performance. A relatively mild recession was a major factor in the staggering collapse of dot-com companies in the early 2000s.

Poor economic conditions make the environment more complex and managers' jobs more difficult and demanding. Managers may need to reduce the number of individuals in their departments and increase the motivation of remaining employees, and managers and workers alike may need to identify ways to acquire and utilize resources more efficiently. Successful managers realize the important effects that economic forces have on their organizations, and they pay close attention to what is occurring in the national and regional economies to respond appropriately.

Technological forces

technology The combination of skills and equipment that managers use in the design, production, and distribution of goods and services.

technological forces Outcomes of changes in the technology that managers use to design, produce, or distribute goods and services.

Technology is the combination of tools, machines, computers, skills, information, and knowledge that managers use in the design, production, and distribution of goods and services. **Technological forces** are outcomes of changes in the technology that managers use to design, produce, or distribute goods and services. The overall pace of technological change has accelerated greatly in the last decade because of advances in microprocessors and computer hardware and software, and technological forces have increased in magnitude.²⁸

Technological forces can have profound implications for managers and organizations, as we discuss in the opening case. Technological change can make established products obsolete—for example, music tape players, typewriters, black-and-white televisions, bound sets of encyclopedias—forcing managers to find new ways to satisfy customer needs. Although technological change can threaten an organization, it also can create a host of new opportunities for designing, making, or distributing new and better kinds of goods and services. More powerful microprocessors, primarily developed by Intel, caused a revolution in information technology that spurred demand for PCs, contributed to the success of companies such as Dell and Compaq, and led to the decline of others such as IBM.²⁹ IBM and other producers of mainframe computers have seen demand for

their products decrease as organizationwide networks of PCs have replaced mainframes in many computing applications.³⁰ However, IBM has responded in the last decade by changing its emphasis from providing computer hardware to providing computer services and consulting and is once again in a strong global position. Managers must move quickly to respond to such changes if their organizations are to survive and prosper; Sony's managers did not, and their company has suffered as a result.

Changes in information technology are altering the very nature of work itself within organizations, including that of the manager's job. Telecommuting along the information superhighway and videoconferencing are now everyday activities that provide opportunities for managers to supervise and coordinate geographically dispersed employees. Salespeople in many companies work from home offices and commute electronically to work. They communicate with other employees through companywide electronic mail networks and use video cameras attached to PCs for "face-to-face" meetings with co-workers who may be across the country.

sociocultural

forces Pressures emanating from the social structure of a country or society or from the national culture.

social structure

The arrangement of relationships between individuals and groups in a society.

national culture

The set of values that a society considers important and the norms of behavior that are approved or sanctioned in that society.

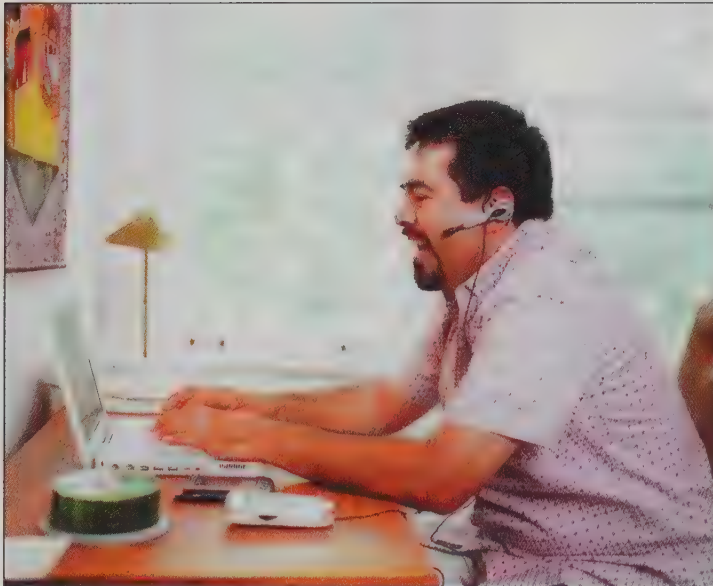
Sociocultural forces

Sociocultural forces are pressures emanating from the social structure of a country or society or from the national culture, pressures that were discussed at length in the previous chapter. Pressures from both sources can either constrain or facilitate the way organizations operate and managers behave. **Social structure** is the arrangement of relationships between individuals and groups in a society. Societies differ substantially in social structure. In societies that have a high degree of social stratification, there are many distinctions among individuals and groups. Caste systems in India and Tibet and the recognition of numerous social classes in Great

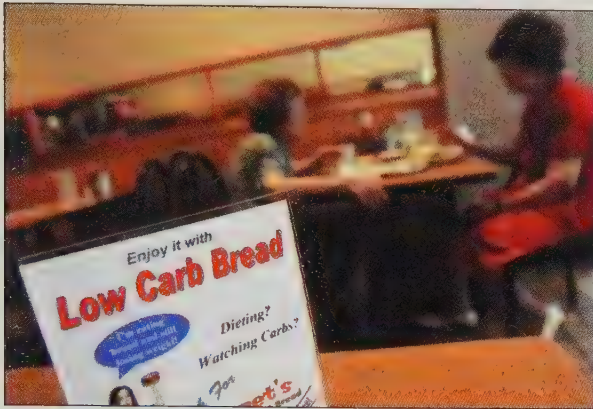
Britain and France produce a multilayered social structure in each of those countries. In contrast, social stratification is lower in relatively egalitarian New Zealand and in the United States, where the social structure reveals few distinctions among people. Most top managers in France come from the upper classes of French society, but top managers in the United States come from all strata of American society.

Societies also differ in the extent to which they emphasize the individual over the group. For example, the United States emphasizes the primacy of the individual, and Japan emphasizes the primacy of the group. This difference may dictate the methods managers need to use to motivate and lead employees.

National culture is the set of values that a society considers important and the norms of behavior that are approved or sanctioned in that society.



In today's wired world, many employees have the option of working from home offices and commuting electronically to work. What do you think some of the challenges might be in supervising and coordinating a group of geographically dispersed employees?



Managers and organizations must respond to social changes within a society. One example is the rage for “low-carb” foods, which affected not only large businesses like Krispy Kreme but also smaller ones such as this local diner.

Societies differ substantially in the values and norms that they emphasize. For example, in the United States individualism is highly valued, and in Korea and Japan individuals are expected to conform to group expectations.³¹ National culture, discussed at length later in this chapter, also affects the way managers motivate and coordinate employees and the way organizations do business. Ethics, an important aspect of national culture, was discussed in detail in Chapter 3.

Social structure and national culture not only differ across societies but also change within societies over time. In the United States, attitudes toward the roles of women, love, sex, and marriage changed in each past decade. Many people in Asian countries such as Hong Kong, Singapore, Korea, and Japan think that the younger generation is far more indi-

vidualistic and “American-like” than previous generations. Currently, throughout much of eastern Europe, new values that emphasize individualism and entrepreneurship are replacing communist values based on collectivism and obedience to the state. The pace of change is accelerating.

Individual managers and organizations must be responsive to changes in, and differences among, the social structures and national cultures of all the countries in which they operate. In today’s increasingly integrated global economy, managers are likely to interact with people from several countries, and many managers live and work abroad. Effective managers are sensitive to differences between societies and adjust their behaviors accordingly.

Managers and organizations also must respond to social changes within a society. In the last few decades, for example, Americans have become increasingly interested in their personal health and fitness. Managers who recognized this trend early and exploited the opportunities that resulted from it were able to reap significant gains for their organizations. PepsiCo used the opportunity presented by the fitness trend and took market share from archrival Coca-Cola by being the first to introduce diet colas and fruit-based soft drinks. Quaker Oats made Gatorade the most popular sports drink and brought out a whole host of low-fat food products. The health trend, however, did not offer opportunities to all companies; to some it posed a threat. Tobacco companies came under intense pressure due to consumers’ greater awareness of negative health impacts from smoking. Hershey Foods and other manufacturers of candy bars have been threatened by customers’ desires for low-fat, healthy foods. The rage for “low-carb” foods in 2004 led to a huge increase in demand for meat and hurt bread and doughnut companies such as Kraft and Krispy Kreme.

demographic

forces Outcomes of changes in, or changing attitudes toward, the characteristics of a population, such as age, gender, ethnic origin, race, sexual orientation, and social class.

Demographic forces

Demographic forces are outcomes of changes in, or changing attitudes toward, the characteristics of a population, such as age, gender, ethnic origin, race, sexual orientation, and social class. Like the other forces in the general environment, demographic forces present managers with opportunities and threats and can have major implications for organizations. We examined the nature of these challenges

in depth in our discussion of diversity in Chapter 3, so we will not discuss these forces again here.

We will just note one important change occurring today: Most industrialized nations are experiencing the aging of their populations as a consequence of falling birth and death rates and the aging of the baby-boom generation. In Germany, for example, the percentage of the population over age 65 is expected to rise to 20.7 percent by 2010 from 15.4 percent in 1990. Comparable figures for Canada are 14.4 and 11.4 percent; for Japan, 19.5 and 11.7 percent; and for the United States, 13.5 and 12.6 percent.³² In the United States the percentage increase is far smaller because of the huge wave of immigration during the 1990s and the large families that new immigrants typically have. However, the absolute number of older people has increased substantially and is increasing opportunities for organizations that cater to older people; the home health care and recreation industries, for example, are seeing an upswing in demand for their services.

The aging of the population also has several implications for the workplace. Most significant are a relative decline in the young people joining the workforce and an increase in the number of active employees willing to postpone retirement past the traditional retirement age of 65. These changes suggest that organizations need to find ways to motivate and utilize the skills and knowledge of older employees, an issue that many Western societies have yet to tackle.

Political and legal forces

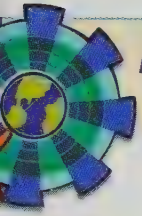
political and legal forces Outcomes of changes in laws and regulations, such as the deregulation of industries, the privatization of organizations, and the increased emphasis on environmental protection.

Political and legal forces are outcomes of changes in laws and regulations. They result from political and legal developments within society and significantly affect managers and organizations. Political processes shape a society's laws. Laws constrain the operations of organizations and managers, and thus create both opportunities and threats.³³ For example, throughout much of the industrialized world there has been a strong trend toward deregulation of industries previously controlled by the state and privatization of organizations once owned by the state.

In the United States, deregulation of the airline industry in 1978 ushered into the task environment of commercial airlines major changes that are still working themselves out. Deregulation allowed 29 new airlines to enter the industry between 1978 and 1993. The increase in airline-passenger carrying capacity after deregulation led to excess capacity on many routes, intense competition, and fare wars. To respond to this more competitive task environment, in the 1980s airlines looked for ways to reduce operating costs. The development of hub-and-spoke systems, the rise of nonunion airlines, and the introduction of no-frills discount service are all responses to increased competition in the airlines' task environment. By the 1990s, once again in control of their environments, airlines were making record profits. However, soaring oil prices in the 2000s wiped out these profits, and airlines found themselves once again under pressure. In 2004, for example, both United Airlines and Delta announced that they were close to bankruptcy, and their futures were uncertain.³⁴

Deregulation and privatization are just two examples of political and legal forces that can challenge organizations and managers. Others include increased emphasis on environmental protection and the preservation of endangered species, increased emphasis on safety in the workplace, and legal constraints against discrimination on the basis of race, gender, or age. Managers who want to take advantage of the

opportunities created by changing global political and legal and economic forces face a major challenge, and nowhere has this been seen more clearly than in the global car industry.



Managing Globally

Car Manufacturing Is Changing Around the World

In the last decade, a huge wave of mergers and alliances between global car manufacturers resulted from changing economic and political conditions. Ford, for example, bought Jaguar and Volvo and owns the majority share in Mazda.³⁵ GM owns Germany's Opel, Sweden's Saab, and Japan's Isuzu; Chrysler and Daimler-Benz merged and bought Mitsubishi in 2000; and Renault bought Nissan in 2000.³⁶

These global mergers occurred because car makers realize that they need to have a strong presence in every region of the world if they are to obtain the full benefits from globalization. Car companies have been merging rapidly to achieve global economies of scale.³⁷ The goal of these companies is to design and produce cars that can be sold throughout the world, making it easier to recoup the huge costs of developing a new vehicle. Also, global car companies can enjoy the low costs that can be obtained from having global supply chains, as discussed earlier. Moreover, they can obtain and share valuable design or car-making skills that may be present in one car company but not in another, such as Mercedes-Benz's safety features or Mitsubishi's low-cost, small-car design skills.

Some of these mergers have been successful. The merger between Renault and Nissan has paid off handsomely as Nissan introduced new global models of cars and SUVs in the 2000s that proved popular around the world; similarly, Ford's merger with Mazda has worked out well.³⁸ Others have been less successful. The DaimlerChrysler and Mitsubishi merger led to no cost savings and proved a disaster; it was announced that the German company was essentially abandoning its links with the Japanese company in 2004. Until 2004, many analysts felt the merger between Daimler-Benz and Chrysler had also been a mistake, as costs rose and the company made record losses. In 2004, however, Chrysler began to introduce many innovative vehicles, so the merger might have a bright future after all. Nevertheless, to date DaimlerChrysler has lost billions from its takeover of Chrysler, as has GM from its investments in Saab and Isuzu.³⁹

Despite their short-term economic problems, however, these mergers are expected to pay off during the next decades as car companies jockey for position as world leaders. Indeed, politically, as the world divides into economic regions, only a global presence will allow a car company to play in the world league. Also, to enter new, largely untapped markets such as eastern Europe and China, car companies have to be able to respond to the different political and cultural forces that characterize business in different countries—hence, the need for operations on a truly global level. Indeed, the takeover of Japanese car companies has been due to the combination of a severe recession in Japan and an increasing political willingness by the Japanese government to allow foreign firms to control Japanese companies.⁴⁰ The same situation is occurring in Korea, where U.S. car companies are targeting bankrupt Korean car companies.

Global forces

global forces

Outcomes of changes in international relationships, changes in nations' economic, political, and legal systems, and changes in technology, such as falling trade barriers, the growth of representative democracies, and reliable and instantaneous communication.

Global forces are outcomes of changes in international relationships, changes in nations' economic, political, and legal systems, and changes in technology. Perhaps the most important global force affecting managers and organizations is the increasing economic integration of countries around the world that has been taking place during the past decades.⁴¹ Free trade agreements such as the General Agreement on Tariffs and Trade (GATT), the North American Free Trade Agreement (NAFTA), and the growth of the European Union (EU) have led to a lowering of barriers to the free flow of goods and services between nations.⁴²

Falling trade barriers have created enormous opportunities for companies in one country to sell goods and services in other countries. By allowing companies from other countries to compete for domestic customers, however, falling trade barriers also pose a serious threat because they increase competition in the task environment. Between 1973 and 2005, for example, U.S. carmakers saw Japanese competitors increase their share of the U.S. car market from 3 to 33 percent.⁴³ This growth would not have been possible without relatively low trade barriers, which allowed producers in Japan to export cars to the United States.

Competition from Toyota, Honda, and other Japanese companies forced managers of the U.S. car companies to find ways to improve their operations. To remain competitive, they had to transform the way their organizations designed and manufactured cars. As a result of these changes, U.S. companies gained ground against their foreign competitors; if they had not, the percentage of foreign cars sold in 2005 in the United States would have been far higher. However, if global forces had not increased the intensity of competition in the task environment of U.S. car companies, U.S. managers might have been slow to make such changes. The U.S. car industry used to be very conservative and slow-moving, but this is no longer the case; it has learned new global values and norms, such as product quality and reliability, for reasons discussed in the next section.

The Changing Global Environment

In the 21st century, any idea that the world is composed of a set of distinct national countries and markets that are separated physically, economically, and culturally from one another has vanished. Managers now recognize that companies exist and compete in a truly global market. Today, managers regard the global environment as a source of important opportunities and threats that they must respond to. Managers constantly confront the challenges of global competition—establishing operations in a country abroad or obtaining inputs from suppliers abroad—or the challenges of managing in a different national culture.⁴⁴ (See Figure 4.3.)

In essence, managers view the global environment as open, that is, as an environment in which they and their organizations are free to buy goods and services from, and sell goods and services to, whichever countries they choose. An open environment is also one in which global organizations are free not only to compete against each other to attract customers but also to establish operations or subsidiaries abroad to become the strongest competitors throughout the world. Coca-Cola and PepsiCo, for example, have competed aggressively for 20 years to develop the strongest global soft-drink empire.



Figure 4.3
The Global Environment

In this section, we explain why the global environment has become more open and competitive and why this development is so significant for managers today. We examine how economic changes such as the lowering of barriers to trade and investment have led to greater interaction and exchanges between organizations and countries. We discuss how declines in barriers of distance and culture have increased the interdependencies between organizations and countries. And we consider the specific implications of these changes for managers and organizations.

Declining barriers to trade and investment

During the 1920s and 1930s, many countries erected formidable barriers to international trade and investment in the belief that this was the best way to promote their economic well-being. Many of these barriers were high tariffs on imports of manufactured goods. A **tariff** is a tax that a government imposes on imported or, occasionally, on exported goods. The aim of import tariffs is to protect domestic industries and jobs, such as those in the auto or steel industry, from foreign competition by raising the price of goods from abroad. In 2001, for example, the U.S. government increased the tariffs on the import of foreign steel to protect U.S. steelmakers; however, under pressure from the European Union, these tariffs were significantly reduced in 2003.

The reason for removing tariffs is that, very often, when one country imposes an import tariff, others follow suit and the result is a series of retaliatory moves as countries progressively raise tariff barriers against each other. In the 1920s this behavior

tariff A tax that a government imposes on imported or, occasionally, exported goods.

depressed world demand and helped usher in the Great Depression of the 1930s and massive unemployment. It was to avoid tariffs on U.S. goods entering Europe that the steel tariffs were reduced. In short, rather than protecting jobs and promoting economic well-being, governments of countries that resort to raising high tariff barriers ultimately reduce employment and undermine economic growth.⁴⁵

GATT AND THE RISE OF FREE TRADE After World War II, advanced Western industrial countries, having learned from the Great Depression, committed themselves to the goal of removing barriers to the free flow of resources between countries. This commitment was reinforced by acceptance of the principle that free trade, rather than tariff barriers, was the best way to foster a healthy domestic economy and low unemployment.⁴⁶

free-trade doctrine

The idea that if each country specializes in the production of the goods and services that it can produce most efficiently, this will make the best use of global resources.

The **free-trade doctrine** predicts that if each country agrees to specialize in the production of the goods and services that it can produce most efficiently, this will make the best use of global resources and will result in lower prices.⁴⁷ For example, if Indian companies are highly efficient in the production of textiles and U.S. companies are highly efficient in the production of computer software, then under a free-trade agreement production of textiles would shift to India and that of computer software to the United States. Consequently, prices of both textiles and software should fall because each good is being produced in the location where it can be made at the lowest cost, benefiting consumers and making the best use of scarce resources. This doctrine is, of course, responsible for the increase in global outsourcing and the loss of millions of U.S. jobs in textiles and manufacturing. However, millions of jobs have been created in high-tech, in IT, and in the service sector that in theory should more than offset these job losses in the long run.

Historically, countries that accepted this free-trade doctrine set as their goal the removal of barriers to the free flow of goods between countries. They attempted to achieve this through an international treaty known as the General Agreement on Tariffs and Trade (GATT). In the half-century since World War II, there have been eight rounds of GATT negotiations aimed at lowering tariff barriers. The last round, the Uruguay Round, involved 117 countries and was completed in December 1993. This round succeeded in lowering tariffs by over 30 percent from the previous level. It also led to the dissolving of GATT and its replacement by the World Trade Organization (WTO), which today continues the struggle to reduce tariffs, and has more power to sanction countries that break global agreements.⁴⁸ On average, the tariff barriers among the governments of developed countries declined from over 40 percent in 1948 to about 3 percent in 2000, causing a dramatic increase in world trade.⁴⁹

Declining barriers of distance and culture

Barriers of distance and culture also closed the global environment and kept managers looking inward. The management problems Unilever, the huge British-based, global soap and detergent maker, experienced at the turn of the 20th century illustrate the effect of these barriers.

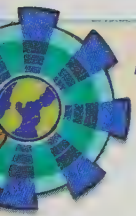
Founded in London during the 1880s by William Lever, a Quaker, Unilever had a worldwide reach by the early 1900s and operated subsidiaries in most major countries of the British Empire, including India, Canada, and Australia. Lever had a very hands-on, autocratic management style and found his far-flung business empire

difficult to control. The reason for Lever's control problems was that communication over great distances was difficult. It took six weeks to reach India by ship from England, and international telephone and telegraph services were very unreliable.

Another problem that Unilever encountered was the difficulty of doing business in societies that were separated from Britain by barriers of language and culture. Different countries have different sets of national beliefs, values, and norms, and Lever found that a management approach that worked in Britain did not necessarily work in India or Persia (now Iran). As a result, management practices had to be tailored to suit each unique national culture. After Lever's death in 1925, top management at Unilever lowered or *decentralized* (see Chapter 7) decision-making authority to the managers of the various national subsidiaries so that they could develop a management approach that suited the country in which they were operating. One result of this strategy was that the subsidiaries grew distant and remote from one another—something that reduced Unilever's performance.⁵⁰

Since the end of World War II, major advances in communications and transportation technology have been reducing the barriers of distance and culture that affected Unilever and other global organizations. Over the last 30 years, global communications have been revolutionized by developments in satellites, digital switching, and optical-fiber telephone lines—and, most recently, by the exploding growth of the Internet and global computer networks. Satellites and optical fibers can carry hundreds of thousands of messages simultaneously, making possible global video teleconferencing and allowing companies to develop global intranets that are company-specific information and decision-making systems.⁵¹

As a result of such developments, reliable, secure, and instantaneous communication is now possible with nearly any location in the world.⁵² Fax machines in Sri Lanka, cellular phones in the Brazilian rain forest, satellite dishes in Russia, video phones in Manhattan, and videoconferencing facilities in Japan are all part of the communications revolution that is changing the way the world works. This revolution has made it possible for a global organization—a tiny garment factory in Li & Fung's network or a huge company such as Nestlé or Unilever—to do business anywhere, anytime, and to search for customers and suppliers around the world. The way in which U.S. retailers have used the possibilities of e-commerce to expand globally is very instructive.



Managing Globally

E-Commerce and Global Customer Responsiveness

The top managers of U.S. dot-com companies such as Amazon.com and eBay were quick to understand the potential of the Internet as a new way to reach customers and create a competitive advantage. These companies' managers quickly built their virtual storefronts and began to offer their products to U.S. customers. Amazon.com, for example, is the acknowledged leader in designing an online storefront that offers its customers an easy-to-use, personalized shopping experience. Its ability to offer customers every book in publication, and at a low price, wiped out thousands of small bookstores throughout the United States. Similarly, eBay's ability to connect buyers and sellers and create a market in which fair prices could be determined revolutionized the auction business.

Given their companies' appeal in the United States, it seemed natural to dot-com managers that they should expand their operations globally to take



Given Amazon's appeal in the United States, it seemed natural to expand operations globally. But dot-com managers discovered that developing a successful global business model takes a great deal of time and money. Creating a virtual storefront such as Amazon's Web site for the Japanese market is only one component of the expansion process. To support this storefront, the company must also build a sophisticated purchasing and distribution network.

advantage of the huge number of potential customers worldwide. They also believed they could develop a global business model quite inexpensively. With the U.S. storefront up and running, all they would need to do was transfer it to an overseas market. There, it could be easily customized to the needs of consumers in a particular country. Amazon.com was particularly aggressive in its expansion plans. In 1996 it established an online bookstore in the United Kingdom; in 1998 it entered the German market; and since then it has entered countries such as Japan and France. Similarly, E*Trade, the stock brokerage and banking company, entered the Japanese market and expanded into Europe.

Developing a successful global business model, however, was much more difficult and expensive than dot-com managers had anticipated. As Amazon.com discovered in the United States, having a successful virtual store is only one of the many pieces of a viable global business model. Creating a sophisticated purchasing and distribution network to get the product to the customer is also vital, and globally this is an

expensive proposition. Indeed, because of the enormous investment needed to establish its overseas operations, Amazon.com could not declare its second quarterly profit until the spring of 2003. Similarly, E*Trade found that customizing its brokerage and banking services to the legal and tax regulations that differ from country to country was much more time-consuming and costly than it expected.

It turned out that the dot-coms that performed the best on a global level were those like Lands' End and Avon that had been catalog sellers. These companies had well-managed overseas sales and distribution networks and were in a strong position to profit from their global networks when they took their catalogs online. Other companies that also performed well were those whose products did not require a high investment in a physical business infrastructure. eBay, for example, provides an electronic platform that links buyers and sellers and allows them to trade. All the actual time and cost involved in shipping products globally is borne by the buyers and sellers, so eBay needed to invest far less in building operations overseas. The job of its managers was to tailor its operating system to the local national culture. Similarly, today most stocks are sold electronically. So companies like E*Trade, which have also created storefronts that match the needs of customers in a particular national culture, seem likely to fare particularly well in the future.

One of the most important innovations in transportation technology that has made the global environment more open has been the growth of commercial jet travel, which reduced the time it takes to get from one location to another. Because of jet travel, New York is now closer to Tokyo than it was to Philadelphia in the days of the 13 colonies—a fact that makes control of far-flung international businesses much easier today than in William Lever's era.

In addition to making travel faster, modern communications and transportation technologies have also helped reduce the cultural distance between countries. The

Internet and its millions of Web sites facilitate the development of global communications networks and media that are helping to create a worldwide culture above and beyond unique national cultures. Moreover, television networks such as CNN, MTV, ESPN, BBC, and HBO can now be received in many countries, and Hollywood films are shown throughout the world.

Effects of free trade on managers

The lowering of barriers to trade and investment and the decline of distance and culture barriers have created enormous opportunities for companies to expand the market for their goods and services through exports and investments in foreign countries. Although managers at some organizations, like Barnes & Noble, have shied away from trying to sell their goods and services overseas, the situation of Wal-Mart and Lands' End, which have developed profitable global operations, is more typical. The shift toward a more open global economy has created not only more opportunities to sell goods and services in markets abroad but also the opportunity to buy more from other countries. Indeed, the success in the United States of Lands' End has been based in part on its managers' willingness to import low-cost clothes and bedding from foreign manufacturers. Lands' End purchases clothing from manufacturers in Hong Kong, Malaysia, Taiwan, and China because U.S. textile makers often do not offer the same quality, styling, flexibility, or price.⁵³ Indeed, most clothing companies such as Levi Strauss, Wal-Mart, and Target are major players in the global environment by virtue of their purchasing activities, even if like Target or Dillard's they sell only in the United States.

The manager's job is more challenging in a dynamic global environment because of the increased intensity of competition that goes hand in hand with the lowering of barriers to trade and investment. Thus, as discussed above, the job of the average manager in a U.S. car company became a lot harder from the mid-1970s on as a result of the penetration of the U.S. market by efficient Japanese competitors. Recall that Levi Strauss closed its last U.S. clothing factory in 2001 because it could not match the prices of low-cost foreign jeans manufacturers that compete with Levi's to sell to clothing chains such as Wal-Mart, Dillard's, and Target.

NAFTA The growth of regional trade agreements such as the North American Free Trade Agreement (NAFTA) also presents opportunities and threats for managers and their organizations. NAFTA, which became effective on January 1, 1994, had the aim of abolishing the tariffs on 99 percent of the goods traded between Mexico, Canada, and the United States by 2004. Although it has not achieved this lofty goal, NAFTA has removed most barriers on the cross-border flow of resources, giving, for example, financial institutions and retail businesses in Canada and the United States unrestricted access to the Mexican marketplace. After NAFTA was signed, there was a flood of investment into Mexico from the United States, as well as many other countries such as Japan. Wal-Mart, Costco, Radio Shack, and other major U.S. retail chains plan to expand their operations in Mexico.

The establishment of free-trade areas creates an opportunity for manufacturing organizations because it allows them to reduce their costs. They can do this either by shifting production to the lowest-cost location within the free-trade area (for example, U.S. auto and textile companies shifting production to Mexico) or by serving the whole region from one location, rather than establishing separate operations in each country.

Some managers, however, might see regional free-trade agreements as a threat because the agreements expose a company based in one member country to increased competition from companies based in the other member countries. Managers in Mexico, the United States, and Canada are experiencing this now through NAFTA. For the first time, Mexican managers find themselves facing a threat: head-to-head competition in some industries against efficient U.S. and Canadian organizations. But the opposite is true as well: U.S. and Canadian managers are experiencing threats in labor-intensive industries, such as the flooring tile and textile industries, where Mexican businesses have a cost advantage.

The three current NAFTA members have announced that they hope to expand the treaty in the future to include countries in Central and South America and thus increase economic prosperity throughout the Americas. Chile is a possible future member, as are Brazil and Argentina. However, the recent currency and economic problems that these countries have been experiencing have slowed down the attempt to expand NAFTA, as has political resistance within the United States because of jobs lost to Mexico and Canada.

In essence, the shift toward a more open, competitive global environment has increased both the opportunities that managers can take advantage of and the threats they must respond to in performing their jobs effectively.

The role of national culture

Despite evidence that countries are becoming more similar to one another and that the world is on the verge of becoming a global village, the cultures of different countries still vary widely because of critical differences in their values, norms, and attitudes. As noted earlier, national culture includes the values, norms, knowledge, beliefs, moral principles, laws, customs, and other practices that unite the citizens of a country.⁵⁴ National culture shapes individual behavior by specifying appropriate and inappropriate behavior and interaction with others. People learn national culture in their everyday lives by interacting with those around them. This learning starts at an early age and continues throughout their lives.

VALUES AND NORMS The basic building blocks of national culture are values and norms. **Values** are ideas about what a society believes to be good, right, desirable, or beautiful. They provide the basic underpinnings for notions of individual freedom, democracy, truth, justice, honesty, loyalty, social obligation, collective responsibility, the appropriate roles for men and women, love, sex, marriage, and so on. Values are more than merely abstract concepts; they are invested with considerable emotional significance. People argue, fight, and even die over values such as freedom.

Although deeply embedded in society, values are not static; however, change in a country's values is likely to be slow and painful. For example, the value systems of many formerly communist states, such as Russia, are undergoing significant changes as those countries move away from a value system that emphasizes the state and toward one that emphasizes individual freedom. Social turmoil often results when countries undergo major changes in their values.

Norms are unwritten rules and codes of conduct that prescribe appropriate behavior in particular situations and shape the behavior of people toward one another. Two types of norms play a major role in national culture: folkways and mores. **Folkways** are the routine social conventions of everyday life. They concern

values Ideas about what a society believes to be good, right, desirable, or beautiful.

norms Unwritten rules and codes of conduct that prescribe how people should act in particular situations.

folkways The routine social conventions of everyday life.



Young Saudi men eat in a fast-food restaurant in Jiddah, Saudi Arabia, March 29, 2002. Saudi Arabia's strict and ascetic interpretation of Islam means movie theaters, nightclubs, and dating are banned. Young Saudis now hang out on the streets, in coffee shops, and fast-food restaurants. Teenagers flash their phone numbers on pieces of cardboard or leave them on bits of paper stuck to car windows, in the hopes of getting a date, even if it is confined to the phone.

mores Norms that are considered to be central to the functioning of society and to social life.

customs and practices such as dressing appropriately for particular situations, good social manners, eating with the correct utensils, and neighborly behavior. Although folkways define the way people are expected to behave, violation of folkways is not a serious or moral matter. People who violate folkways are often thought to be eccentric or ill-mannered, but they are not usually considered to be evil or bad. In many countries, initially foreigners may be excused for violating folkways because they are unaccustomed to local behavior, but repeated violations are not excused because foreigners are expected to learn appropriate behavior.

Mores are norms that are considered to be central to the functioning of society and to social life. They have much greater significance than folkways. Accordingly, the violation of mores can be expected to bring serious retribution. Mores include proscriptions against theft, adultery, and incest. In many societies mores have been enacted into law. Thus, all

advanced societies have laws against theft and incest. However, there are many differences in mores from one society to another.⁵⁵ In the United States, for example, drinking alcohol is widely accepted; but in Saudi Arabia, the consumption of alcohol is viewed as a violation of social norms and is punishable by imprisonment (as many U.S. citizens working in Saudi Arabia have discovered).

Hofstede's model of national culture

Researchers have spent considerable time and effort identifying similarities and differences in the values and norms of different countries. One model of national culture was developed by Geert Hofstede.⁵⁶ As a psychologist for IBM, Hofstede collected data on employee values and norms from more than 100,000 IBM employees in 64 countries. Based on his research, Hofstede developed five dimensions along which national cultures can be placed (see Figure 4.4).⁵⁷

individualism A worldview that values individual freedom and self-expression and adherence to the principle that people should be judged by their individual achievements rather than by their social background.

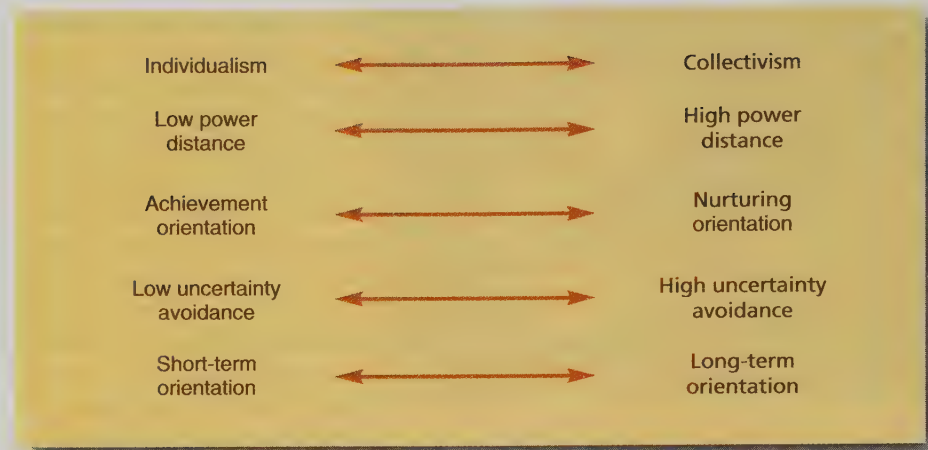
collectivism A worldview that values subordination of the individual to the goals of the group and adherence to the principle that people should be judged by their contribution to the group.

INDIVIDUALISM VERSUS COLLECTIVISM The first dimension, which Hofstede labeled "individualism versus collectivism," has a long history in human thought. **Individualism** is a worldview that values individual freedom and self-expression and adherence to the principle that people should be judged by their individual achievements rather than by their social background. In Western countries, individualism usually includes admiration for personal success, a strong belief in individual rights, and high regard for individual entrepreneurs.⁵⁸

In contrast, **collectivism** is a worldview that values subordination of the individual to the goals of the group and adherence to the principle that people should be judged by their contribution to the group. Collectivism was widespread in communist countries but has become less prevalent since the collapse of communism in most of those countries. Japan is a noncommunist country where collectivism is highly valued.

Collectivism in Japan traces its roots to the fusion of Confucian, Buddhist, and Shinto thought that occurred during the Tokugawa period in Japanese history

Figure 4.4
Hofstede's
Model of
National Culture



Source: *Administrative Science Quarterly*, Geert Hofstede, Bram Nevijen, Denise Daval Ohayv, and Geert Sanders, *Measuring Organizational Cultures: A Qualitative and Quantitative Study Across Twenty Cases*, Volume 35, Number 2 (June 1990), pp. 286–316. Approval of Request for Permission to Reprint. © Johnson Graduate School of Management, Cornell University.

(1600–1870s).⁵⁹ One of the central values that emerged during this period was strong attachment to the group—whether a village, a work group, or a company. Strong identification with the group is said to create pressures for collective action in Japan, as well as strong pressure for conformity to group norms and a relative lack of individualism.⁶⁰

Managers must realize that organizations and organizational members reflect their national culture's emphasis on individualism or collectivism. Indeed, one of the major reasons why Japanese and American management practices differ is that Japanese culture values collectivism and U.S. culture values individualism.⁶¹

power distance The degree to which societies accept the idea that inequalities in the power and well-being of their citizens are due to differences in individuals' physical and intellectual capabilities and heritage.

POWER DISTANCE By **power distance** Hofstede meant the degree to which societies accept the idea that inequalities in the power and well-being of their citizens are due to differences in individuals' physical and intellectual capabilities and heritage. This concept also encompasses the degree to which societies accept the economic and social differences in wealth, status, and well-being that result from differences in individual capabilities.

Societies in which inequalities are allowed to persist or grow over time have *high power distance*. In high-power-distance societies, workers who are professionally successful amass wealth and pass it on to their children, and, as a result, inequalities may grow over time. In such societies, the gap between rich and poor, with all the attendant political and social consequences, grows very large. In contrast, in societies with *low power distance*, large inequalities between citizens are not allowed to develop. In low-power-distance countries, the government uses taxation and social welfare programs to reduce inequality and improve the welfare of the least fortunate. These societies are more attuned to preventing a large gap between rich and poor and minimizing discord between different classes of citizens.

Advanced Western countries such as the United States, Germany, the Netherlands, and the United Kingdom have relatively low power distance and high individualism. Economically poor Latin American countries such as Guatemala and Panama, and Asian countries such as Malaysia and the Philippines, have high power

achievement orientation

A worldview that values assertiveness, performance, success, and competition.

nurturing orientation

A worldview that values the quality of life, warm personal friendships, and services and care for the weak.

uncertainty avoidance

The degree to which societies are willing to tolerate uncertainty and risk.

long-term orientation

A worldview that values thrift and persistence in achieving goals.

short-term orientation

A worldview that values personal stability or happiness and living for the present.

distance and low individualism.⁶² These findings suggest that the cultural values of richer countries emphasize protecting the rights of individuals and, at the same time, provide a fair chance of success to every member of society.

ACHIEVEMENT VERSUS NURTURING ORIENTATION Societies that have an **achievement orientation** value assertiveness, performance, success, competition, and results. Societies that have a **nurturing orientation** value the quality of life, warm personal relationships, and services and care for the weak. Japan and the United States tend to be achievement-oriented; the Netherlands, Sweden, and Denmark are more nurturing-oriented.

UNCERTAINTY AVOIDANCE Societies as well as individuals differ in their tolerance for uncertainty and risk. Societies low on **uncertainty avoidance** (such as the United States and Hong Kong) are easygoing, value diversity, and tolerate differences in personal beliefs and actions. Societies high on uncertainty avoidance (such as Japan and France) are more rigid and skeptical about people whose behaviors or beliefs differ from the norm. In these societies, conformity to the values of the social and work groups to which a person belongs is the norm, and structured situations are preferred because they provide a sense of security.

LONG-TERM VERSUS SHORT-TERM ORIENTATION The last dimension that Hofstede described is orientation toward life and work.⁶³ A national culture with a **long-term orientation** rests on values such as thrift (saving) and persistence in achieving goals. A national culture with a **short-term orientation** is concerned with maintaining personal stability or happiness and living for the present. Societies with a long-term orientation include Taiwan and Hong Kong, well known for their high rate of per capita savings. The United States and France have a short-term orientation, and their citizens tend to spend more and save less.

National culture and global management

Differences among national cultures have important implications for managers. First, because of cultural differences, management practices that are effective in one country might be troublesome in another. General Electric's managers learned this while trying to manage Tungsram, a Hungarian lighting products company it acquired for \$150 million. GE was attracted to Tungsram, widely regarded as one of Hungary's best companies, because of Hungary's low wage rates and the possibility of using the company as a base from which to export lighting products to western Europe. GE transferred some of its best managers to Tungsram and hoped it would soon become a leader in Europe. Unfortunately, many problems arose.

One of the problems resulted from major misunderstandings between the American managers and the Hungarian workers. The Americans complained that the Hungarians were lazy; the Hungarians thought the Americans were pushy. The Americans wanted strong sales and marketing functions that would pamper customers. In the prior command economy, sales and marketing activities were unnecessary. In addition, Hungarians expected GE to deliver Western-style wages, but GE came to Hungary to take advantage of the country's low-wage structure.⁶⁴ As Tungsram's losses mounted, GE managers had to admit that, because of differences in basic attitudes between countries, they had underestimated the difficulties they

would face in turning Tungsram around. Nevertheless, by 2001, these problems had been solved, and the increased efficiency of GE's Hungarian operations made General Electric a major player in the European lighting market, causing it to invest another \$1 billion.⁶⁵

Often, management practices must be tailored to suit the cultural contexts within which an organization operates. An approach effective in the United States might not work in Japan, Hungary, or Mexico because of differences in national culture. For example, U.S.-style pay-for-performance systems that emphasize the performance of individuals alone might not work well in Japan, where individual performance in pursuit of group goals is the value that receives emphasis.

Managers doing business with individuals from another country must be sensitive to the value systems and norms of that country and behave accordingly. For example, Friday is the Islamic Sabbath. Thus, it would be impolite and inappropriate for a U.S. manager to schedule a busy day of activities for Saudi Arabian managers visiting on a Friday.

A culturally diverse management team can be a source of strength for an organization participating in the global marketplace. Organizations that employ managers from a variety of cultures appreciate better than do organizations with culturally homogeneous management teams how national cultures differ, and they tailor their management systems and behaviors to the differences. Indeed, one of the advantages that many Western companies have over their Japanese competitors is greater willingness to build an international team of senior managers.⁶⁶

Summary and Review

WHAT IS THE ORGANIZATIONAL ENVIRONMENT?

The organizational environment is the set of forces and conditions that operate beyond an organization's boundaries but affect a manager's ability to acquire and utilize resources. The organizational environment has two components, the task environment and the general environment.

THE TASK ENVIRONMENT The task environment is the set of forces and conditions that originate with suppliers, distributors, customers, and competitors that influence managers on a daily basis. The opportunities and threats associated with forces in the task environment become more complex as a company begins to operate in more than one country and expands globally.

THE GENERAL ENVIRONMENT The general environment is wider-ranging economic, technological, sociocultural, demographic, political and legal, and global forces that affect an organization and its task environment.

THE CHANGING GLOBAL ENVIRONMENT In recent years there has been a marked shift away from a closed global environment, in which countries are cut off from one another by barriers to international trade and investment and by barriers of distance and culture, and toward a more open global environment. The emergence of an open global environment and the reduction of barriers to the free flow of goods, services, and investment owe much to the rise of global trade agreements such as GATT, to the growing global acceptance of a free-market philosophy, and to the poor performance of countries that protected their markets from international trade and investment.



Management in Action

Topics for Discussion and Action

Discussion

1. Why is it important for managers to understand the nature of the environmental forces that are acting on them and their organization?
2. Which organization is likely to face the most complex task environment, a biotechnology company trying to develop a new cure for cancer or a large retailer like The Gap or Macy's? Why?
3. The population is aging because of declining birth rates, declining death rates, and the aging of the baby-boom generation. What might some of the implications of this demographic trend be for
(a) a pharmaceutical company, (b) the home construction industry?
4. How do political, legal, and economic forces shape national culture? What characteristics of national culture do you think have the most important effect on how successful a country is in doing business abroad?
5. After the passage of the North American Free Trade Agreement, many U.S. companies shifted production operations to Mexico to take advantage of lower labor costs and lower standards for environmental and worker protection. As a result, they

cut their costs and were better able to survive in an increasingly competitive global environment. Was their behavior ethical—that is, did the ends justify the means?

Action

6. Choose an organization, and ask a manager in that organization to list the number and strengths of forces in the organization's task environment. Ask the manager to pay particular attention to identifying opportunities and threats that result from pressures and changes in customers, competitors, and suppliers.

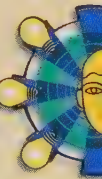


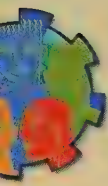
Building Management Skills

Analyzing an Organization's Task and General Environments

Pick an organization with which you are familiar. It can be an organization in which you have worked or currently work or one that you interact with regularly as a customer (such as the college that you are currently attending). For this organization do the following:

1. Describe the main forces in the task environment that are affecting the organization.
2. Describe the main forces in the general environment that are affecting the organization.
3. Describe the main global forces that are affecting the organization.
4. Explain how environmental forces affect the job of an individual manager within this organization. How do they determine the opportunities and threats that its managers must confront?





Small Group Breakout Exercise

How to Enter the Copying Business

Form groups of three to five people, and appoint one group member as the spokesperson who will communicate your findings to the whole class when called on by the instructor. Then discuss the following scenario.

You and your partners have decided to open a small printing and copying business in a college town of 100,000 people. Your business will compete with companies like Kinko's. You know that over 50 percent of small businesses fail in their first year, so to increase your chances of success, you have decided to do a detailed analysis of

the task environment of the copying business to discover what opportunities and threats you will encounter. As a group:

1. Decide what you must know about (a) your future customers, (b) your future competitors, and (c) other critical forces in the task

environment if you are to be successful.

2. Evaluate the main barriers to entry into the copying business.
3. Based on this analysis, list some of the steps you would take to help your new copying business succeed.



Be the Manager

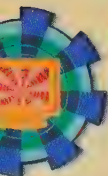
You are the new manager of a major clothing store that is facing a crisis. This clothing store has been the leader in its market for the last 15 years. In the last three years, however, two other major clothing store chains have opened up, and they have steadily been attracting customers away from your store—your sales are down 30 percent. To find out why, your store surveyed former customers and learned that they perceive the store as not keeping up with changing fashion trends and

new forms of customer service. In examining the way the store operates, you found out that the 10 purchasing managers who buy the clothing and accessories for the store have been buying increasingly from the same clothing suppliers and have become reluctant to try new ones. Moreover, salespeople rarely, if ever, make suggestions for changing the way the store operates, they don't respond to customer requests, and the culture of the store has become conservative and risk-averse.

The Changing Environment of Retailing

Questions

1. Analyze the major forces in the task environment of a retail clothing store.
2. Devise a program that will help other managers and employees to better understand and respond to their store's task environment.



Additional Activities on the Build Your Management Skills DVD

- **Test Your Knowledge:**
 - (1) Macroenvironmental Forces and (2) Hofstede's Model of National Culture
- **Manager's Hot Seat:** Cultural Differences: Let's Break a Deal

Managing Ethically

In recent years, the number of U.S. companies that buy their inputs from low-cost foreign suppliers has been growing, and concern about the ethics associated with employing young children in factories has been increasing. In Pakistan and India, children as young as six years old work long hours to make rugs and carpets for export to Western countries or clay bricks for local use. In countries like Malaysia

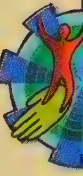
and in Central America, children and teenagers routinely work long hours in factories and sweat shops to produce the clothing that is found in most U.S. discount and department stores.

Questions

1. Either by yourself or in a group, discuss whether it is ethical to employ children in factories and whether U.S.

companies should buy and sell products made by these children. What are some arguments for and against child labor?

2. If child labor is an economic necessity, what ways could be employed to make it as ethical a practice as possible? Or is it simply unethical?



BusinessWeek

Case in the News

The Vanishing Mass Market

To most of us, Tide is as familiar as home. Last year, Americans bought some \$2 billion worth of Tide, which has ranked as the country's biggest-selling laundry detergent ever since Procter & Gamble Co. took it national in 1949. If ever a brand epitomized the great, one-size-fits-all mass market, it is Tide, right? Wrong. Or so says Procter & Gamble itself. James R. Stengel, P&G's global marketing officer, insists that his company's bulging portfolio of big brands contains "not one mass-market brand, whether it's Tide or Old Spice"—or Crest or Pampers or Ivory. "Every one of our brands is targeted."

In the boom decades after World War II, it was P&G more than any other company that put the mass in marketing, relying on TV commercials and print ads to flog its standardized wares from coast to coast. Along with Coca-Cola, McDonald's, General Motors, Unilever Group,

American Express, and many other consumer-products giants, P&G now is standing mass marketing on its head by shifting emphasis from selling to the vast, anonymous crowd to selling to millions of particular consumers. "You find the people. You are very focused on them," Stengel says. "You become relevant to them."

For marketers, the evolution from mass to micromarketing is a fundamental change driven as much by necessity as opportunity. America today is a far more diverse and commercially self-indulgent society than it was in the heyday of the mass market. The country has atomized into countless market segments defined not only by demography, but by increasingly nuanced and insistent product preferences. "All the research we're doing tells us that the driver of demand going forward is all about products that are 'right for me,'"

says David Martin, president of Interbrand Corp. "And that's ultimately about offering a degree of customization for all."

At the same time, the almost-universal audience assembled long ago by network television and augmented by the other mass media is fragmenting at an accelerating rate. The mass media's decline is an old story in many respects; prime-time network ratings and newspaper circulation have been sliding since the 1970s. What's new is that the proliferation of digital and wireless communication channels is spreading the mass audience of yore ever-thinner across hundreds of narrowcast cable-TV and radio channels, thousands of specialized magazines, and millions of computer terminals, video-game consoles, personal digital assistants, and cell-phone screens.

In the 1960s, an advertiser could reach 80 percent of U.S.

women with a spot aired simultaneously on CBS, NBC, and ABC. Today, an ad would have to run on 100 TV channels to have a prayer of duplicating this feat. Adding a few Web sites would help, but not even the biggest new media conduits—not Home Box Office, not Yahoo, not AOL Instant Messenger, not even X-Box—is likely to ever match

the ubiquity of the Big Three networks in their prime.

Questions

1. How do changes in the mass market affect the task environment facing organizations?

2. How can companies respond to the changes taking place?

Source: Anthony Bianco, Tom Lowry, Robert Berner, Michael Arndt, and Ronald Grover, "The Vanishing Mass Market." Reprinted from the July 12, 2004, issue of *BusinessWeek* by special permission. Copyright © 2004 by the McGraw-Hill Companies.

BusinessWeek

Case in the News

Posco: One Sharp Steelmaker

Korea these days enjoys a well-deserved reputation for its digital prowess: A land where lab-coated engineers and scientists work with delicate wafer chips, while pink-haired youths write software for the latest cell phone. But you don't have to dig too deep to find another Korea, one where hard-bodied workers labor in factories to produce the stuff that makes the physical world go. To get an idea of the vibrancy of this part of the economy, visit the Posco steelworks in Pohang, on the peninsula's east coast. Here, in sweltering heat, sparks fly as molten iron is ladled into vast bins, and ribbons of fiery metal roll through milling machines.

Old Economy? Sure. But Posco is no rust-belt relic. True, with \$12 billion in sales, it isn't the biggest steelmaker on earth. That title belongs to Luxembourg-based Arcelor, more than double Posco's size. But where it really counts, Posco is in a class all its own. The company enjoys the biggest profits in the global steel industry, raking in enough cash to make many a high-tech outfit envious. Thanks to robust demand at home and in China, net

earnings from Posco's array of steel products—used in everything from screws to skyscrapers—last year shot up 80 percent, to \$1.66 billion. And Daewoo Securities Co. is forecasting a 61 percent jump in profits, to \$2.7 billion, on \$15.6 billion in sales this year. "As far as efficiency is concerned, Posco stands taller than any other steelmaker in the world," says Daewoo analyst Yang Ki In.

In fact, Posco isn't as different from South Korea's New Economy innovators as all the sweat and sparks might lead you to believe. The company is considered one of the industry's high-tech paladins. In August 2004, Posco enhanced that reputation when it broke ground on a \$1.1 billion mill that could boost productivity even higher. The mill will use a new technology, called Finex, that will help cut costs by nearly a fifth and harmful emissions by more than 90 percent, says Chairman and CEO Lee Ku Taek. For decades, steelmakers have used highly polluting ovens to turn powdery coal and iron ore into chunks called coke and sinter, which are melted with superheated

air to make iron. With Finex, coal and ore are turned into iron without coking and sintering. After the plant opens, in about two years, Posco plans to roll out the technology in other mills. "I want to be remembered as the CEO who started another leap forward," says Lee, a 35-year Posco veteran who has become the project's champion since taking over the top job a year ago.

Posco has put plenty of slick information technology to work, too. The company has invested \$179 million to network its 80 Korean plants so that it can take orders online and coordinate production and deliveries. So, as molten steel slabs wend their way through the mills at Posco's two major steelworks—in Pohang and at Gwangyang, on the southern coast—each is pressed to a specified weight and width depending on a particular customer's needs. This mill-level customization helps push steel out the door faster, which has enabled Posco to halve delivery times and slash inventories by 60 percent.

Like the rest of Korea Inc., Posco believes its future lies across the Yellow Sea in China. The country

has become the world's biggest steel market as well as the biggest producer, with more than 1,000 mills, from giants such as Shanghai BaoSteel Group and Wuhan Iron & Steel Group to tiny operations in outlying provinces. To cash in on this vast opportunity, Posco has invested \$800 million in China, its biggest export market. One joint venture, with Benxi Iron & Steel (Group) Co., near Shenyang, will churn out 1.8 million tons of cold-rolled sheets annually for autos

and home appliances when it opens in 2006. Another, with Jiangsu Shagang Group, already produces 280,000 tons of stainless cold-rolled coils and some 100,000 tons of galvanized steel every year. In all, Posco has 14 joint ventures in China. By 2006, Posco plans some \$1.4 billion in fresh investment on the mainland, especially in galvanized and stainless steel to supply global auto and appliance makers that have opened plants there.

Questions

1. In what ways is Posco responding to the changing forces in its task environment?
2. In what ways is Posco responding to the changing forces in its general environment?

Source: Brian Bremmer, Moon Ihlwan, and Dexter Roberts, "Posco: One Sharp Steelmaker." Reprinted from the August 30, 2004, issue of *BusinessWeek* by special permission. Copyright © 2004 by the McGraw-Hill Companies.

CHAPTER

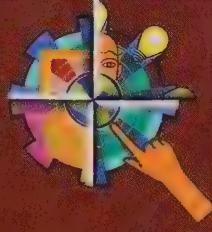
5

Decision Making, Learning, Creativity, and Innovation

Learning Objectives

After studying this chapter, you should be able to:

- Differentiate between programmed and nonprogrammed decisions, and explain why nonprogrammed decision making is a complex, uncertain process.
- Describe the six steps that managers should take to make the best decisions.
- Identify the advantages and disadvantages of group decision making, and describe techniques that can improve it.
- Explain the role that organizational learning and creativity play in helping managers to improve their decisions.



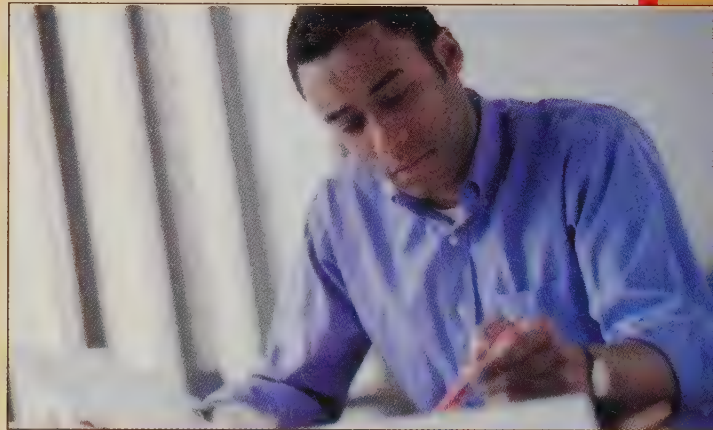
Management Snapshot

Revising Decisions and Plans Never Ends for Craig Knouf

Why is managerial decision making often fraught with uncertainty? Having a good business plan outlining key decisions is essential for entrepreneurs to obtain funding from banks, venture capitalists, and other sources of funds. Once entrepreneurs have secured funding and their businesses are up and running, the decisions in their business plans are typically reviewed only once a year as part of an annual planning process, unless, of course, the entrepreneurs are seeking to obtain additional funds. However, these decisions and business plans are inherently fraught with uncertainty, as is starting a new business and having it actually succeed. Viewing a business plan as a work in progress that should be evolving on an almost continuous basis has turned out to be a blessing for Craig Knouf, founder, CEO, and majority owner of Associated Business Systems (ABS), a Portland, Oregon, supplier of office equipment.¹

Knouf estimates that he has revised his decisions and business plan over 120 times since founding ABS in 1997; he makes a point of reviewing and, if necessary, revising ABS's

business plan on a monthly basis after consulting with the firm's seven vice presidents. As Knouf puts it, "If you only looked at the plan every quarter, by the time you realize the mistake, you're five months off. . . . You're done.



A business plan is best viewed as a work-in-progress.

You're not going to get back on track."² Of course, the reason why managers like Knouf have to continually rethink their decisions is the inherent uncertainty in all that they do. As a case in point, in the early years Knouf never anticipated that scanners would be a significant part of his business. But during his monthly reviews of the business, he noticed that sales of office equipment with scanning

capabilities were steadily increasing. Acting on what his sales data were telling him, Knouf decided to quickly add products with scanning capabilities to his company's offerings, and by 2004 sales of these products were over \$3 million.³

Knouf's ability to appreciate the inherent uncertainty of the best-made plans and decisions, and the benefit of frequently changing courses of action in response to feedback from customers and the market, has certainly paid off handsomely for his company. Since its founding in 1997, ABS's revenues have grown from \$880,000 to over \$20 million.⁴ ABS appeared on *Inc.* magazine's list of fastest-growing private companies in 2002 and 2003 and was on the *Portland Business Journal*'s list of fastest-growing companies in Oregon from 1999 to 2003.⁵ In 2004, ABS was listed as both one of Oregon's top private companies by *Oregon Business* and

one of Oregon's best companies to work for by *Oregon Business Magazine*.⁶ Even suppliers have taken notice of ABS's ability to stay in touch with the market, provide excellent, timely service to customers, and actively respond to changing market conditions.⁷ For example, ABS was one of only eight distributors across the United States selected by Hewlett-Packard to launch a new line of high-speed copiers with multiple functions such as printing and scanning.⁸ Management experts agree that Knouf's approach to decision making and planning makes good business sense. As Eric Siegel, Wharton Business School lecturer and president of Siegel Management Consultants, puts it, "The world turns; things change. . . . What you commit to a document on Dec. 19 is not necessarily appropriate on Jan. 19."⁹

Overview

The "Management Snapshot" illustrates how important decision making is in organizations and also how decision making is often fraught with uncertainty. In this chapter, we examine how managers make decisions and explore how individual, group, and organizational factors affect the quality of the decisions they make and ultimately determine organizational performance. We discuss the nature of managerial decision making and examine some models of the decision-making process that help reveal the complexities of successful decision making. Then we outline the main steps of the decision-making process. Finally, we examine how managers can promote organizational learning, creativity, and innovation and improve the quality of decision making throughout an organization. By the end of this chapter, you will appreciate the critical role decision making plays in creating a high-performing organization.

The Nature of Managerial Decision Making

Every time managers act to plan, organize, direct, or control organizational activities, they make a stream of decisions. In opening a new restaurant, for example, managers have to decide where to locate it, what kinds of food to provide to customers, which people to employ, and so on. Decision making is a basic part of every task managers perform.

As we discussed in the last chapter, one of the main tasks facing a manager is to manage the organizational environment. Forces in the external environment give rise to many opportunities and threats for managers and their organizations. In addition, inside an organization managers must address many opportunities and threats that may arise during the course of utilizing organizational resources. To deal with these opportunities and threats, managers must make decisions—that is,

decision making

The process by which managers respond to opportunities and threats by analyzing options and making determinations about specific organizational goals and courses of action.

they must select one solution from a set of alternatives. **Decision making** is the process by which managers respond to the opportunities and threats that confront them by analyzing the options and making determinations, or *decisions*, about specific organizational goals and courses of action. Good decisions result in the selection of appropriate goals and courses of action that increase organizational performance; bad decisions result in lower performance.

Decision making in response to opportunities occurs when managers search for ways to improve organizational performance to benefit customers, employees, and other stakeholder groups. In the “Management Snapshot,” Craig Knouf saw an opportunity in selling office equipment with scanning capabilities. *Decision making in response to threats* occurs when events inside or outside the organization are adversely affecting organizational performance and managers are searching for ways to increase performance.¹⁰ Decision making is central to being a manager, and whenever managers engage in planning, organizing, leading, and controlling—their four principal functions—they are constantly making decisions.

Managers are always searching for ways to make better decisions to improve organizational performance. At the same time, they do their best to avoid costly mistakes that will hurt organizational performance. Examples of spectacularly good decisions include Liz Claiborne’s decision in the 1980s to focus on producing clothes for the growing number of women entering the workforce—a decision that contributed to making her company one of the largest clothing manufacturers. Also, Bill Gates’s decision to buy a computer operating system for \$50,000 from a small company in Seattle and sell it to IBM for the new IBM personal computer turned Gates and Microsoft, respectively, into the richest man and richest software company in the United States. Examples of spectacularly bad decisions include the decision by managers at NASA and Morton Thiokol to launch the *Challenger* space shuttle—a decision that resulted in the deaths of six astronauts in 1986. Also, the decision of Ken Olsen, founder of Digital Equipment Corporation, to stay with mainframe computers in the 1980s and not allow his engineers to spend the company’s resources on creating new kinds of personal computers because of his belief that “personal computers are just toys” was a decision that cost Olsen his job as CEO and almost ruined his company.

Programmed and nonprogrammed decision making

Regardless of the specific decisions that a manager makes, the decision-making process is either programmed or nonprogrammed.¹¹

programmed decision making

Routine, virtually automatic decision making that follows established rules or guidelines.

PROGRAMMED DECISION MAKING **Programmed decision making** is a *routine*, virtually automatic process. Programmed decisions are decisions that have been made so many times in the past that managers have developed rules or guidelines to be applied when certain situations inevitably occur. Programmed decision making takes place when a school principal asks the school board to hire a new teacher whenever student enrollment increases by 40 students; when a manufacturing supervisor hires new workers whenever existing workers’ overtime increases by more than 10 percent; and when an office manager orders basic office supplies, such as paper and pens, whenever the inventory of supplies on hand drops below a

certain level. Furthermore, in the last example, the office manager probably orders the same amount of supplies each time.

This decision making is called *programmed* because office managers, for example, do not need to repeatedly make new judgments about what should be done. They can rely on long-established decision rules such as these:

- *Rule 1:* When the storage shelves are three-quarters empty, order more copy paper.
- *Rule 2:* When ordering paper, order enough to fill the shelves.

Managers can develop rules and guidelines to regulate all routine organizational activities. For example, rules can specify how a worker should perform a certain task, and rules can specify the quality standards that raw materials must meet to be acceptable. Most decision making that relates to the day-to-day running of an organization is programmed decision making. Examples include decision making about how much inventory to hold, when to pay bills, when to bill customers, and when to order materials and supplies. Programmed decision making occurs when managers have the information they need to create rules that will guide decision making. There is little ambiguity involved in assessing when the stockroom is empty or counting the number of new students in class.

NONPROGRAMMED DECISION MAKING Suppose, however, managers are not at all certain that a course of action will lead to a desired outcome. Or, in even more ambiguous terms, suppose managers are not even clear about what they are really trying to achieve. Obviously, rules cannot be developed to predict uncertain events. **Nonprogrammed decision making** is required for these nonroutine decisions. Nonprogrammed decisions are made in response to unusual or novel opportunities and threats. Nonprogrammed decision making occurs when there are no ready-made decision rules that managers can apply to a situation. Rules do not exist because the situation is unexpected or uncertain and managers lack the information they would need to develop rules to cover it. Examples of nonprogrammed decision making include decisions to invest in a new kind of technology, develop a new kind of product, launch a new promotional campaign, enter a new market, expand internationally, or start a company as did Knouf in the “Management Snapshot.”

How do managers make decisions in the absence of decision rules? They may rely on their **intuition**—feelings, beliefs, and hunches that come readily to mind, require little effort and information gathering, and result in on-the-spot decisions.¹² Or they may make **reasoned judgments**—decisions that take time and effort to make and result from careful information gathering, generation of alternatives, and evaluation of alternatives. “Exercising” one’s judgment is a more rational process than “going with” one’s intuition. For reasons that we examine later in this chapter, both intuition and judgment often are flawed and can result in poor decision making. Thus, the likelihood of error is much greater in nonprogrammed decision making than in programmed decision making.¹³ In the remainder of this chapter, when we talk about decision making, we are referring to *nonprogrammed* decision making because it causes the most problems for managers and is inherently challenging.

Sometimes managers have to make rapid decisions and don’t have the time for careful consideration of the issues involved. They must rely on their intuition

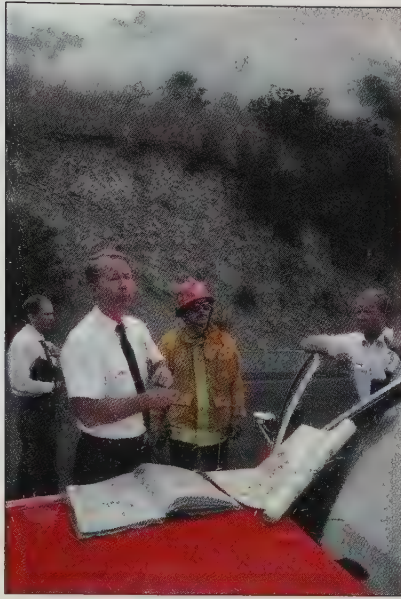
nonprogrammed decision making

Nonroutine decision making that occurs in response to unusual, unpredictable opportunities and threats.

intuition Feelings, beliefs, and hunches that come readily to mind, require little effort and information gathering, and result in on-the-spot decisions.

reasoned judgment

A decision that takes time and effort to make and results from careful information gathering, generation of alternatives, and evaluation of alternatives.



Fire chiefs and firefighters gather to plan strategy at the scene of a brush fire in Los Angeles's Griffith Park. In a crisis like this, managers don't have much time for decision making and, therefore, must rely on their expert intuition.

to quickly respond to a pressing concern. For example, when fire chiefs, captains, and lieutenants manage firefighters battling dangerous, out-of-control fires, they often need to rely on their expert intuition to make on-the-spot decisions that will protect the lives of the firefighters and save the lives of others, contain the fires, and preserve property—decisions made in emergency situations entailing high uncertainty, high risk, and rapidly changing conditions.¹⁴ Other times, managers do have the time available to make reasoned judgments but there are no established rules to guide their decisions, such as when deciding whether or not to proceed with a proposed merger. Regardless of the circumstances, making nonprogrammed decisions can result in effective or ineffective decision making. As indicated in the following “Manager as a Person,” managers have to be on their guard to avoid being overconfident in decisions that result from their intuition and reasoned judgment.

Manager as a Person

Curbing Overconfidence

Should managers be confident in their intuition and reasoned judgments?¹⁵ Decades of research by Nobel Prize winner Daniel Kahneman, his long-time collaborator the late Amos Tversky, and other researchers suggests that, if anything, managers (like all people) tend to be overconfident in the decisions they make (whether based on intuition or reasoned judgments). And with overconfidence comes the failure to evaluate and rethink the wisdom of the decisions one makes and to learn from mistakes.¹⁶

Kahneman distinguishes between the intuitions of managers who are truly expert in the content domain of a decision and the intuition of managers who have some knowledge and experience but are not true experts.¹⁷ While the intuition of both types can be faulty, that of experts is less likely to be flawed. This is why fire captains can make good decisions and why expert chess players can make good moves, in both cases without spending much time, and deliberate carefully on what, for nonexperts, is a very complicated set of circumstances. What distinguishes expert managers from those with “some” expertise is that the experts have extensive experience under conditions in which they receive quick and clear feedback about the outcomes of their decisions.¹⁸

Unfortunately, managers who have some experience in a content area but are not true experts tend to be overly confident in their intuition and their judgments.¹⁹ As Kahneman puts it, “People jump to statistical conclusions on the basis of very weak evidence. We form powerful intuitions about trends and about the replicability of results on the basis of information that is truly inadequate.”²⁰

Not only do managers, and all people, tend to be overconfident about their intuitions and judgments, but they also tend not to learn from mistakes. Compounding this undue optimism is a very human tendency to be overconfident in one's own abilities and influence over unpredictable events. Surveys have found that the majority of people think they are above average, make better decisions, and are less prone to making bad decisions than others (of course, it is impossible for most people to be above average on any dimension).²¹

A recent example of managerial overconfidence is particularly telling. Research has consistently found that mergers tend to turn out poorly—post-merger profitability declines, stock prices decline, and so forth. (For example, Chrysler had the biggest profits of the three largest automobile makers in the United States when it merged with Daimler; the merger has not worked out well and Chrysler would have been better off if it never had happened.) So one would imagine that top executives and boards of directors would learn from this research and from articles in the business press about the woes of merged companies (e.g., the AOL–Time Warner merger). Evidently not. According to a recent study by Hewitt Associates, top executives and board members are, if anything, planning on increasing their involvement in mergers over the next few years. These top managers evidently overconfidently believe that they can succeed where others have failed.²²

Jeffrey Pfeffer, a professor at Stanford University's Graduate School of Business, suggests that managers can avoid the perils of overconfidence by critically evaluating the decisions they have made and the outcomes of those decisions. They should admit to themselves when they have made a mistake and really learn from their mistakes (rather than dismissing them as flukes or situations out of their control). In addition, managers should be leery of too much agreement at the top. As Pfeffer puts it, "If two people agree all the time, one of them is redundant."²³

classical decision-making model

A prescriptive approach to decision making based on the assumption that the decision maker can identify and evaluate all possible alternatives and their consequences and rationally choose the most appropriate course of action.

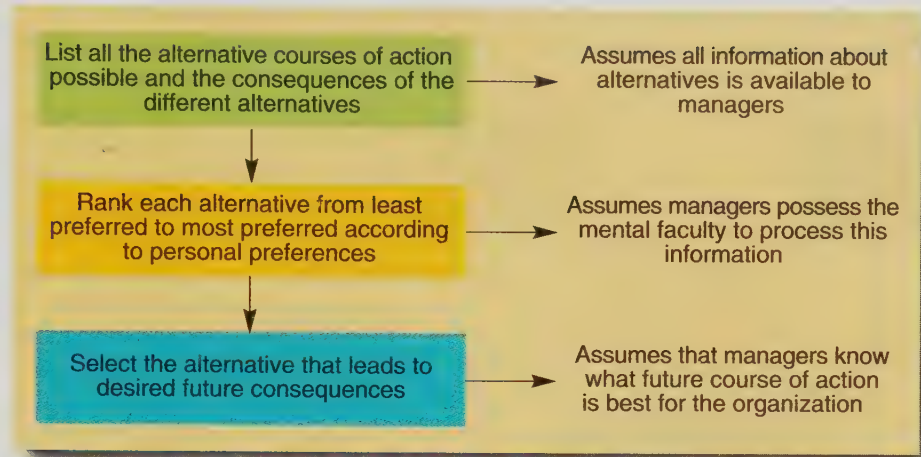
optimum decision

The most appropriate decision in light of what managers believe to be the most desirable future consequences for the organization.

The classical and the administrative decision-making models reveal many of the assumptions, complexities, and pitfalls that affect decision making. These models help reveal the factors that managers and other decision makers must be aware of to improve the quality of their decision making. Keep in mind, however, that the classical and administrative models are just guides that can help managers understand the decision-making process. In real life, the process is typically not cut-and-dried, but these models can help guide a manager through it.

The classical model

One of the earliest models of decision making, the **classical model**, is *prescriptive*, which means that it specifies how decisions *should* be made. Managers using the classical model make a series of simplifying assumptions about the nature of the decision-making process (see Figure 5.1). The premise of the classical model is that once managers recognize the need to make a decision, they should be able to generate a complete list of all alternatives and consequences and make the best choice. In other words, the classical model assumes that managers have access to *all* the information they need to make the **optimum decision**, which is the most appropriate decision possible in light of what they believe to be the most desirable future

Figure 5.1**The Classical Model of Decision Making**

consequences for the organization. Furthermore, the classical model assumes that managers can easily list their own preferences for each alternative and rank them from least to most preferred to make the optimum decision.

The administrative model

James March and Herbert Simon disagreed with the underlying assumptions of the classical model of decision making. In contrast, they proposed that managers in the real world do *not* have access to all the information they need to make a decision. Moreover, they pointed out that even if all information were readily available, many managers would lack the mental or psychological ability to absorb and evaluate it correctly. As a result, March and Simon developed the **administrative model** of decision making to explain why decision making is always an inherently uncertain and risky process—and why managers can rarely make decisions in the manner prescribed by the classical model. The administrative model is based on three important concepts: bounded rationality, incomplete information, and satisficing.

administrative model

An approach to decision making that explains why decision making is inherently uncertain and risky and why managers usually make satisfactory rather than optimum decisions.

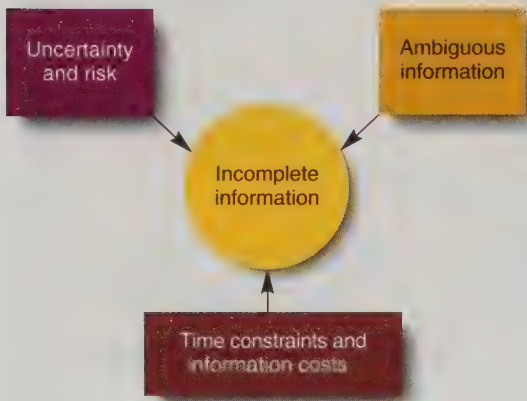
bounded

rationality Cognitive limitations that constrain one's ability to interpret, process, and act on information.

BOUNDED RATIONALITY March and Simon pointed out that human decision-making capabilities are bounded by people's cognitive limitations—that is, limitations in their ability to interpret, process, and act on information.²⁴ They argued that the limitations of human intelligence constrain the ability of decision makers to determine the optimum decision. March and Simon coined the term **bounded rationality** to describe the situation in which the number of alternatives a manager must identify is so great and the amount of information so vast that it is difficult for the manager to even come close to evaluating it all before making a decision.²⁵

INCOMPLETE INFORMATION Even if managers did have an unlimited ability to evaluate information, they still would not be able to arrive at the optimum decision because they would have incomplete information. Information is incomplete because the full range of decision-making alternatives is unknowable in most situations and the consequences associated with known alternatives are uncertain. In other words, information is incomplete because of risk and uncertainty, ambiguity, and time constraints (see Figure 5.2).

Figure 5.2
Why Information is Incomplete



risk The degree of probability that the possible outcomes of a particular course of action will occur.

uncertainty
Unpredictability.

ambiguous information

Information that can be interpreted in multiple and often conflicting ways.

comes are *unknown*. Managers are working blind. Since the probability of a given outcome occurring is *not* known, managers have little information to use in making a decision. For example, in 1993, when Apple Computer introduced the Newton, its personal digital assistant (PDA), managers had no idea what the probability of a successful product launch for a PDA might be. Because Apple was the first to market this totally new product, there was no body of well-known data that Apple's managers could draw on to calculate the probability of a successful launch.



When Apple introduced the Newton, shown here, managers were working under conditions of extreme uncertainty. Because Apple was the first to market this type of product, there was no body of well-known data that managers could draw on to calculate the probability of a successful product launch.

RISK AND UNCERTAINTY As we saw in Chapter 4, forces in the organizational environment are constantly changing. **Risk** is present when managers know the possible outcomes of a particular course of action and can assign probabilities to them. For example, managers in the biotechnology industry know that new drugs have a 10 percent probability of successfully passing advanced clinical trials and a 90 percent probability of failing. These probabilities reflect the experiences of thousands of drugs that have gone through advanced clinical trials. Thus, when managers in the biotechnology industry decide to submit a drug for testing, they know that there is only a 10 percent chance that the drug will succeed, but at least they have some information on which to base their decision.

When **uncertainty** exists, the probabilities of alternative outcomes *cannot* be determined and future outcomes are *unknown*. Managers are working blind. Since the probability of a given outcome occurring is *not* known, managers have little information to use in making a decision. For example, in 1993, when Apple Computer introduced the Newton, its personal digital assistant (PDA), managers had no idea what the probability of a successful product launch for a PDA might be. Because Apple was the first to market this totally new product, there was no body of well-known data that Apple's managers could draw on to calculate the probability of a successful launch. Uncertainty plagues most managerial decision making.²⁶ Although Apple's initial launch of its PDA was a disaster due to technical problems, an improved version was more successful. In fact, Apple created the PDA market that has boomed during the 2000s as new and different wireless products have been introduced.

AMBIGUOUS INFORMATION A second reason why information is incomplete is that much of the information managers have at their disposal is **ambiguous information**. Its meaning is not clear—it can be interpreted in multiple and often conflicting ways.²⁷ Take a look at Figure 5.3. Do you see a young woman or an old woman? In a similar fashion, managers often interpret the same piece of information differently and make decisions based on their own interpretations.

TIME CONSTRAINTS AND INFORMATION COSTS The third reason why information is incomplete is that managers have neither the time nor the money to search for all possible alternative solutions and evaluate all the potential consequences of those alternatives. Consider the situation

Figure 5.3**Ambiguous Information:
Young Woman or Old Woman?****satisficing**

Searching for and choosing an acceptable, or satisfactory, response to problems and opportunities, rather than trying to make the best decision.

confronting a Ford Motor Company purchasing manager who has one month to choose a supplier for a small engine part. Of the thousands of potential suppliers for this part, there are 20,000 in the United States alone. Given the time available, the purchasing manager cannot contact all potential suppliers and ask each for its terms (price, delivery schedules, and so on). Moreover, even if the time were available, the costs of obtaining the information, including the manager's own time, would be prohibitive.

SATISFICING March and Simon argue that managers do not attempt to discover every alternative when faced with bounded rationality, an uncertain future, unquantifiable risks, considerable ambiguity, time constraints, and high information costs. Rather, they use a strategy known as **satisficing**, exploring a limited sample of all potential alternatives.²⁸ When managers satisfice, they search for and choose acceptable, or satisfactory, ways to respond to problems and opportunities rather than trying to make the optimal decision.²⁹ In the case of the Ford purchasing manager's search, for example, satisficing may involve asking a limited number of suppliers for their terms, trusting that they are representative of suppliers in general, and making a choice from that set. Although this course of action is reasonable from the perspective of the purchasing manager, it may mean that a potentially superior supplier is overlooked.

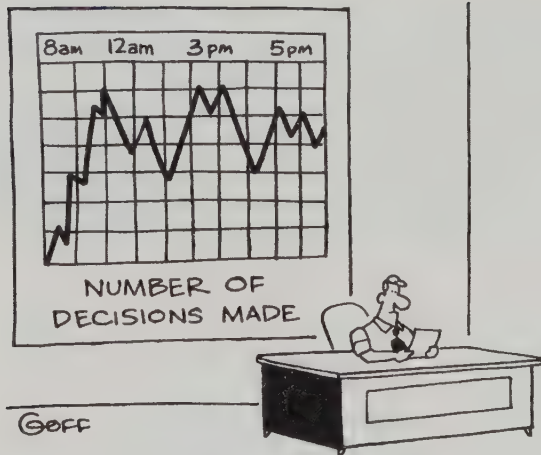
March and Simon pointed out that managerial decision making is often more art than science. In the real world, managers must rely on their intuition and judgment to make what seems to them to be the best decision in the face of uncertainty and ambiguity.³⁰

Moreover, managerial decision making is often fast-paced, as managers use their experience and judgment to make crucial decisions under conditions of incomplete information. Although there is nothing wrong with this approach, decision makers should be aware that human judgment is often flawed. As a result, even the best managers sometimes end up making very poor decisions.³¹

Steps in the Decision-Making Process

Using the work of March and Simon as a basis, researchers have developed a step-by-step model of the decision-making process and the issues and problems that managers confront at each step. Perhaps the best way to introduce this model is to examine the real-world nonprogrammed decision making that Scott McNealy had to engage in at a crucial point in Sun Microsystems' history.

In early August 1985, Scott McNealy, CEO of Sun Microsystems³² (a hardware and software computer workstation manufacturer focused on network solutions), had to decide whether to go ahead with the launch of the new Carrera workstation computer, scheduled for September 10. Sun's managers had chosen the date nine months earlier when the development plan for the Carrera was first proposed. McNealy knew that it would take at least a month to prepare for the September 10 launch and that the decision could not be put off.



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Customers were waiting for the new machine, and McNealy wanted to be the first to provide a workstation that took advantage of Motorola's powerful 16-megahertz 68020 microprocessor. Capitalizing on this opportunity would give Sun a significant edge over Apollo, its main competitor in the workstation market. McNealy knew, however, that committing to the September 10 launch date was risky. Motorola was having production problems with the 16-megahertz 68020 microprocessor and could not guarantee Sun a steady supply of these chips. Moreover, the operating system software was not completely free of bugs.

If Sun launched the Carrera on September 10, the company might have to ship some machines with software that was not fully operational, was prone to crash the system, and utilized Motorola's less-powerful 12-megahertz 68020 microprocessor instead of the 16-megahertz version.³³ Of course, Sun could later upgrade the microprocessor and operating system software in any machines purchased by early customers, but the company's reputation would suffer as a result. If Sun did not go ahead with the September launch, the company would miss an important opportunity.³⁴ Rumors were circulating in the industry that Apollo would be launching a new machine of its own in December. McNealy wondered what he should do. The microprocessor and operating system problems might be resolved by September 10, but then again they might not be.

Scott McNealy clearly had a difficult decision to make. He had to decide quickly whether to launch the Carrera, but he was not in possession of all the facts. He did not know, for example, whether the microprocessor or operating system problems could be resolved by September 10; nor did he know whether Apollo was going to launch a competing machine in December. But he could not wait to find these things out—he had to make a decision. We'll see what he decided later in the chapter.

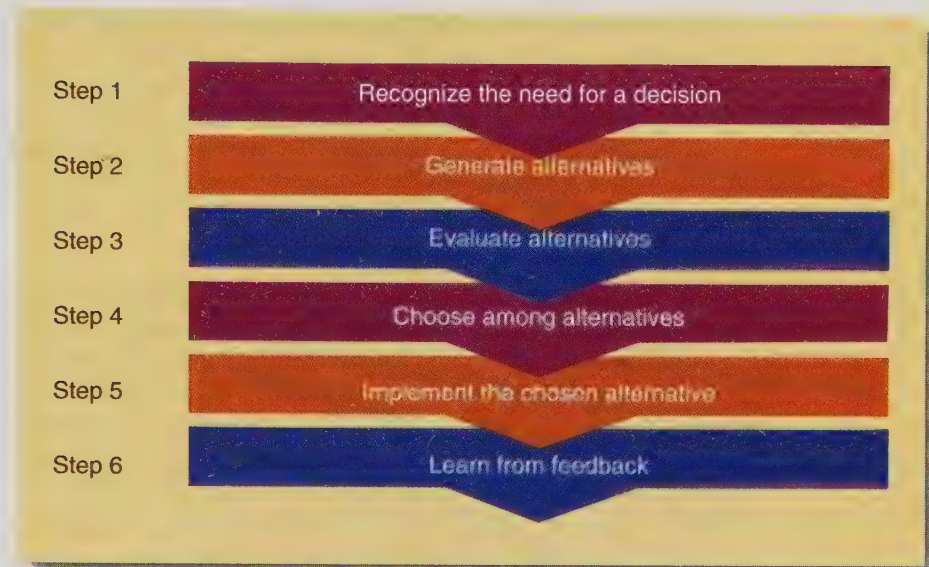
Many managers who must make important decisions with incomplete information face dilemmas similar to McNealy's. There are six steps that managers should consciously follow to make a good decision (see Figure 5.4).³⁵ We review them in the remainder of this section.

Recognize the need for a decision

The first step in the decision-making process is to recognize the need for a decision. Scott McNealy recognized this need, and he realized that a decision had to be made quickly because it would take a month to get ready for the September 10 launch. McNealy also knew that the September 10 launch was a critical goal because Sun needed to beat Apollo to the market with a new machine to gain a competitive advantage over this strong challenger.

Some stimuli usually spark the realization that there is a need to make a decision. These stimuli often become apparent because changes in the organizational environment result in new kinds of opportunities and threats. This happened at Sun Microsystems. The September 10 launch date had been set when it seemed that Motorola chips would be readily available. Later, with the supply of chips in doubt

Figure 5.4
Six Steps in
Decision Making



and bugs remaining in the system software, Sun was in danger of failing to meet its launch date.

The stimuli that spark decision making are as likely to result from the actions of managers inside an organization as they are from changes in the external environment.³⁶ An organization possesses a set of skills, competencies, and resources in its employees and in departments such as marketing, manufacturing, and research and development. Managers who actively pursue opportunities to use these competencies create the need to make decisions. Managers thus can be proactive or reactive in recognizing the need to make a decision, but the important issue is that they must recognize this need and respond in a timely and appropriate way.³⁷

Generate alternatives

Having recognized the need to make a decision, a manager must generate a set of feasible alternative courses of action to take in response to the opportunity or threat. Management experts cite failure to properly generate and consider different alternatives as one reason why managers sometimes make bad decisions.³⁸ In the Sun Microsystems decision, the alternatives seem clear: to go ahead with the September 10 launch or to delay the launch until the Carrera was 100 percent ready for market introduction. Often, however, the alternatives are not so obvious or so clearly specified.

One major problem is that managers may find it difficult to come up with creative alternative solutions to specific problems. Perhaps some of them are used to seeing the world from a single perspective—they have a certain “managerial mind-set.” In a manner similar to that of Digital’s Olsen, many managers find it difficult to view problems from a fresh perspective. According to best-selling management author Peter Senge, we all are trapped within our personal mental models of the world—our ideas about what is important and how the world works.³⁹ Generating creative alternatives to solve problems and take advantage of opportunities may require that we abandon our existing mind-sets and develop new ones—something that usually is difficult to do.

The importance of getting managers to set aside their mental models of the world and generate creative alternatives is reflected in the growth of interest in the work of authors such as Peter Senge and Edward de Bono, who have popularized techniques for stimulating problem solving and creative thinking among managers.⁴⁰ Later in this chapter, we discuss the important issues of organizational learning and creativity in detail.

Evaluate alternatives

Once managers have generated a set of alternatives, they must evaluate the advantages and disadvantages of each one.⁴¹ The key to a good assessment of the alternatives is to define the opportunity or threat exactly and then specify the criteria that should influence the selection of alternatives for responding to the problem or opportunity. One reason for bad decisions is that managers often fail to specify the criteria that are important in reaching a decision.⁴² In general, successful managers use four criteria to evaluate the pros and cons of alternative courses of action (see Figure 5.5):

1. *Legality.* Managers must ensure that a possible course of action is legal and will not violate any domestic and international laws or government regulations.
2. *Ethicalness.* Managers must ensure that a possible course of action is ethical and will not unnecessarily harm any stakeholder group. Many of the decisions that managers make may help some organizational stakeholders and harm others (see Chapter 3). When examining alternative courses of action, managers need to be very clear about the potential effects of their decisions.
3. *Economic feasibility.* Managers must decide whether the alternatives are economically feasible—that is, whether they can be accomplished given the organization's performance goals. Typically, managers perform a cost-benefit analysis of the various alternatives to determine which one will have the best net financial payoff.
4. *Practicality.* Managers must decide whether they have the capabilities and resources required to implement the alternative, and they must be sure that the alternative will not threaten the attainment of other organizational goals. At first glance, an alternative might seem to be economically superior to other alternatives, but if managers realize that it is likely to threaten other important projects, they might decide that it is not practical after all.

Very often, a manager must consider these four criteria simultaneously. Scott McNealy framed the problem at hand at Sun Microsystems quite well. The key question was whether to go ahead with the September 10 launch date. Two main criteria were influencing McNealy's choice: the need to ship a machine that was as "complete" as possible (the *practicality* criterion) and the need to beat Apollo to market with a new workstation (the *economic feasibility* criterion). These two criteria conflicted. The first suggested that the launch should be delayed; the second, that the launch should go ahead. McNealy's actual choice was based on the relative importance that he assigned to these two criteria. In fact, Sun Microsystems went ahead with the September 10 launch, which suggests that McNealy thought the need to beat Apollo to market was the more important criterion.

Some of the worst managerial decisions can be traced to poor assessment of the alternatives, such as the decision to launch the *Challenger* space shuttle, mentioned earlier. In that case, the desire of NASA and Morton Thiokol managers to demonstrate to the public the success of the U.S. space program in order to ensure future funding (*economic feasibility*) conflicted with the need to ensure the safety of the

Figure 5.5
General Criteria
for Evaluating
Possible
Courses of
Action



astronauts (*ethicalness*). Managers deemed the economic criterion more important and decided to launch the space shuttle even though there were unanswered questions about safety. Tragically, some of the same decision-making problems that resulted in the *Challenger* tragedy led to the demise of the *Columbia* space shuttle in 2003, 17 years later, killing all seven astronauts on board.⁴³

Ethics in Action

NASA's Flawed Culture

Seventeen years after the *Challenger* disaster, history repeated itself on February 1, 2003, when *Columbia* broke up over Texas on the final day of its mission, killing all seven astronauts on board.⁴⁴ While different specific causes resulted in each of these tragedies, they were both at least partially the result of a deeper, more widespread problem: a flawed safety culture at NASA, where concerns with budgets and schedules were emphasized at the expense of safety.⁴⁵

Both the Columbia Accident Investigation Board (CAIB) and a NASA team headed by Al Diaz, director of the Goddard Space Flight Center, concluded—after intensive investigations involving employees at all ranks, outside contractors, and engineering and scientific data—that NASA's flawed, can-do culture, emphasizing budgets and schedules over safety, was partially to blame for the *Columbia* tragedy.⁴⁶ Commenting on the CAIB report and their own investigations, the Diaz team stated:

Had the fate of STS-107 been the result of a small number of well-defined problems in a single program, finding solutions would be a relatively straightforward matter. But the CAIB determined that such is not the case. . . . It was their conclusion that the mistakes made on STS-107 were not isolated failures but rather were indicative of systemic flaws that existed prior to the accident. The Diaz Team believes that some of these systemic flaws exist beyond the shuttle program.⁴⁷



The Columbia crew wave to onlookers on their way to the launch pad for liftoff. Leading the way are Pilot William "Willie" McCool (left) and Commander Rick Husband. Following in the second row are Mission Specialists Kalpana Chawla (left) and Laurel Clark; in the rear are Payload Specialist Ilan Ramon (left), Payload Commander Michael Anderson, and Mission Specialist David Brown. Ramon was the first astronaut from Israel to fly on a shuttle.

the organization's culture.⁵² Among other things, he is trying to improve communication, encourage all employees to speak up without fear of retribution, make sure that all employees' inputs are heard, ensure that technical expertise is taken into account when making decisions, and, above all, emphasize safety.⁵³ Currently, NASA engineers are trying to develop fillers and wrappings that astronauts can use to repair unexpected cracks, gashes, and holes on shuttles during space flights.⁵⁴ And efforts are under way to prevent foam insulation from breaking off fuel tanks when shuttles are launched.⁵⁵ Above all else, Parsons is trying to change the culture so that safety is a top priority, technical expertise is respected, and shuttles are not launched until all known problems are addressed.⁵⁶

In both the *Challenger* and the *Columbia* disasters, safety questions were raised before the shuttles were launched; safety concerns took second place to budgets, economic feasibility, and schedules; top decision makers seemed to ignore or downplay the inputs of those with relevant technical expertise; and speaking up was discouraged.⁴⁸ Rather than making safety a top priority, decision makers seemed overly concerned with keeping on schedule and within budget.⁴⁹ The day before *Columbia* lifted off, mission managers were presented with data indicating that a ring that linked the rocket boosters to the external tank failed to meet strength requirements. Rather than postponing the launch to address this problem, a shuttle manager temporarily waived the requirements based on what later turned out to be faulty data.⁵⁰ After foam had broken loose the next day during liftoff (a recurring problem) and struck the left wing, NASA engineers repeatedly and doggedly requested that images of the area in which the foam had struck be obtained to assess the extent of the damage and perhaps plan a rescue mission. Mission managers actively opposed their requests, and no images were obtained.⁵¹

Bill Parsons, who now heads the troubled shuttle program, is committed to changing

Choose among alternatives

Once the set of alternative solutions has been carefully evaluated, the next task is to rank the various alternatives (using the criteria discussed in the previous section) and make a decision. When ranking alternatives, managers must be sure *all* the information available is brought to bear on the problem or issue at hand. As the Sun Microsystems case indicates, however, identifying all *relevant* information for a decision does not mean that the manager has *complete* information; in most instances, information is incomplete.

Perhaps more serious than the existence of incomplete information is the often-documented tendency of managers to ignore critical information, even when it is available. We discuss this tendency in detail below when we examine the operation of cognitive biases and groupthink.

Implement the chosen alternative

Once a decision has been made and an alternative has been selected, it must be implemented, and many subsequent and related decisions must be made. After a course of action has been decided—say, to develop a new line of women’s clothing—thousands of subsequent decisions are necessary to implement it. These decisions would involve recruiting dress designers, obtaining fabrics, finding high-quality manufacturers, and signing contracts with clothing stores to sell the new line.

Although the need to make subsequent decisions to implement the chosen course of action may seem obvious, many managers make a decision and then fail to act on it. This is the same as not making a decision at all. To ensure that a decision is implemented, top managers must assign to middle managers the responsibility for making the follow-up decisions necessary to achieve the goal. They must give middle managers sufficient resources to achieve the goal, and they must hold the middle managers accountable for their performance. If the middle managers are successful at implementing the decision, they should be rewarded; if they fail, they should be subject to sanctions.

Learn from feedback

The final step in the decision-making process is learning from feedback. Effective managers always conduct a retrospective analysis to see what they can learn from past successes or failures. Managers who do not evaluate the results of their decisions do not learn from experience; instead, they stagnate and are likely to make the same mistakes again and again.⁵⁷ To avoid this problem, managers must establish a formal procedure with which they can learn from the results of past decisions. The procedure should include these steps:

1. Compare what actually happened to what was expected to happen as a result of the decision.
2. Explore why any expectations for the decision were not met.
3. Derive guidelines that will help in future decision making.

Managers who always strive to learn from past mistakes and successes are likely to continuously improve the decisions they make. A significant amount of learning can take place when the outcomes of decisions are evaluated, and this assessment can produce enormous benefits.

Group Decision Making

Many, perhaps most, important organizational decisions are made by groups or teams of managers rather than by individuals. Group decision making is superior to individual decision making in several respects. When managers work as a team to make decisions and solve problems, their choices of alternatives are less likely to fall victim to the biases and errors discussed previously. They are able to draw on the combined skills, competencies, and accumulated knowledge of

group members and thereby improve their ability to generate feasible alternatives and make good decisions. Group decision making also allows managers to process more information and to correct one another's errors. And in the implementation phase, all managers affected by the decisions agree to cooperate. When a group of managers makes a decision (as opposed to one top manager making a decision and imposing it on subordinate managers), the probability that the decision will be implemented successfully increases. (We discuss how to encourage employee participation in decision making in Chapter 10.) Advances in information technology can facilitate the group decision-making process, as indicated in the following "Information Technology Byte."

Information Technology Byte

Improving Medical Decision Making

Physicians and medical professionals are often skeptical about the ability of advances in information technology to improve medical decision making. Dr. John Halamka is on a mission to change this.⁵⁸ In 1998, Halamka became chief information officer (CIO) for CareGroup, a company that owns hospitals in the Boston area.⁵⁹ Two of the hospitals owned by CareGroup had merged a few years earlier to form Beth Israel Deaconess Hospital, and the merger was proving to be a financial drain. The two hospitals had different computer systems, a patient who had been to each of the hospitals would have two different ID numbers, many records were handwritten, and files often had to be walked from one hospital to the other.⁶⁰ The inability to access and share information across and within the hospitals hampered decision making.

When Halamka, an emergency room physician, became CIO, he decided to develop an integrated IT system to improve decision making and reduce medical errors at Beth Israel Deaconess. Given CareGroup's financial woes, funds were tight, so Halamka and a team of three developers designed and wrote the code for the system themselves.⁶¹ Implementing the system was a real challenge, as physicians tend to resist using computers in their medical practices for a variety of reasons. Originally, the IT system focused on medical records, and later it was expanded to computerize doctors' orders. The system saved CareGroup money and also reduced medical errors.⁶² For example, doctors' orders and dosages could be checked against patient records to ensure they were correct and there were no incompatibilities; doctors, nurses, and pharmacies could easily share information; and all patient records could be accessed by any member of a health care team as needed via computer.⁶³



Integrated IT systems can save medical providers money and, more importantly, reduce medical errors.

For Joe S., who recently made a trip to Beth Israel's emergency room at the urging of his wife, the IT system

was a life saver. Joe felt dizzy and was having a bit of trouble breathing but otherwise felt fine. Using the IT system, emergency room doctors were able to access Joe's medical history, including an EKG from a year earlier, which they compared with a current EKG. Being able to make this instant comparison (and not having to wait to retrieve and compare actual films) saved Joe's life: Based on the EKG comparisons, his doctors correctly determined that Joe was having a heart attack and were able to immediately race him to the cardiac unit, where he was administered anticoagulants and a blocked artery was opened through angioplasty.

Unfortunately, many hospitals do not have the kind of IT system that enables doctors to view a patient's medical records on the spot. Halamka is on a mission to change that. As he puts it, "IT saves money, and that's very important. . . . But in the end, the lives that it saves is why every single hospital system has to embrace this stuff."⁶⁴

There are some potential disadvantages associated with group decision making. Groups often take much longer than individuals to make decisions. Getting two or more managers to agree to the same solution can be difficult because managers' interests and preferences are often different. In addition, just like decision making by individual managers, group decision making can be undermined by biases. A major source of group bias is *groupthink*.

The perils of groupthink

groupthink A pattern of faulty and biased decision making that occurs in groups whose members strive for agreement among themselves at the expense of accurately assessing information relevant to a decision.

Groupthink is a pattern of faulty and biased decision making that occurs in groups whose members strive for agreement among themselves at the expense of accurately assessing information relevant to a decision.⁶⁵ When managers are subject to groupthink, they collectively embark on a course of action without developing appropriate criteria to evaluate alternatives. Typically, a group rallies around one central manager, such as the CEO, and the course of action that manager supports. Group members become blindly committed to that course of action without evaluating its merits. Commitment is often based on an emotional, rather than an objective, assessment of the optimal course of action.

The decision President Kennedy and his advisers made to launch the unfortunate Bay of Pigs invasion in Cuba in 1962, the decisions made by President Johnson and his advisers from 1964 to 1967 to escalate the war in Vietnam, the decision made by President Nixon and his advisers in 1972 to cover up the Watergate break-in, and the decision made by NASA and Morton Thiokol in 1986 to launch the ill-fated *Challenger* shuttle, which exploded after takeoff—all were likely influenced by groupthink. After the fact, decision makers such as these who may fall victim to groupthink are often surprised that their decision-making process and outcomes were so flawed.

When groupthink occurs, pressures for agreement and harmony within a group have the unintended effect of discouraging individuals from raising issues that run counter to majority opinion. For example, when managers at NASA and Morton Thiokol fell victim to groupthink, they convinced each other that all was well and that there was no need to delay the launch of the *Challenger* space shuttle.

Devil's advocacy

The existence of cognitive biases and groupthink raises the question of how to improve the quality of group and individual decision making so that managers make decisions that are realistic and are based on a thorough evaluation of alternatives. One technique known to counteract groupthink is devil's advocacy.⁶⁶

devil's advocacy

Critical analysis of a preferred alternative, made in response to challenges raised by a group member who, playing the role of devil's advocate, defends unpopular or opposing alternatives for the sake of argument.

Devil's advocacy is a critical analysis of a preferred alternative to ascertain its strengths and weaknesses before it is implemented.⁶⁷ Typically, one member of the decision-making group plays the role of devil's advocate. The devil's advocate critiques and challenges the way the group evaluated alternatives and chose one over the others. The purpose of devil's advocacy is to identify all the reasons that might make the preferred alternative unacceptable after all. In this way, decision makers can be made aware of the possible perils of recommended courses of action.

Diversity among decision makers

Another way to improve group decision making is to promote diversity in decision-making groups (see Chapter 3).⁶⁸ Bringing together managers of both genders from various ethnic, national, and functional backgrounds broadens the range of life experiences and opinions that group members can draw on as they generate, assess, and choose among alternatives. Moreover, diverse groups are sometimes less prone to groupthink because group members already differ from each other and thus are less subject to pressures for uniformity.

Organizational Learning and Creativity

The quality of managerial decision making ultimately depends on innovative responses to opportunities and threats. How can managers increase their ability to make nonprogrammed decisions, decisions that will allow them to adapt to, modify, and even drastically alter their task environments so that they can continually increase organizational performance? The answer is by encouraging organizational learning.⁶⁹

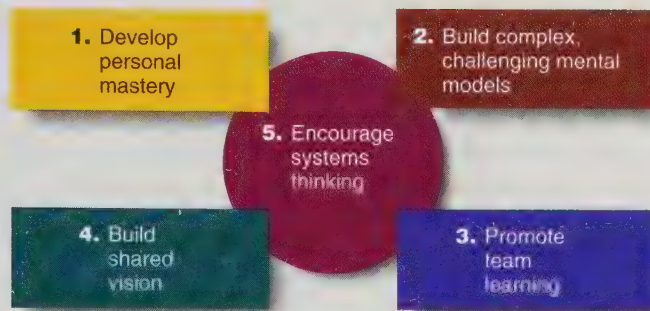
organizational learning

The process through which managers seek to improve employees' desire and ability to understand and manage the organization and its task environment.

Organizational learning is the process through which managers seek to improve employees' desire and ability to understand and manage the organization and its task environment so that employees can make decisions that continuously raise organizational effectiveness.⁷⁰ A **learning organization** is one in which managers do everything possible to maximize the ability of individuals and groups to think and behave creatively and thus maximize the potential for organizational learning to take place. At the heart of organizational learning is **creativity**, the ability of a decision maker to discover original and novel ideas that lead to feasible alternative courses of action. When new and useful ideas are implemented in an organization, **innovation** takes place. Encouraging creativity among managers is such a pressing organizational concern that many organizations hire outside experts to help them develop programs to train their managers in the art of creative thinking and problem solving.

Creating a learning organization

How do managers go about creating a learning organization? Learning theorist Peter Senge identified five principles for creating a learning organization (see Figure 5.6).⁷¹

Figure 5.6**Senge's Principles for Creating a Learning Organization****learning**

organization An organization in which managers try to maximize the ability of individuals and groups to think and behave creatively and thus maximize the potential for organizational learning to take place.

creativity A decision maker's ability to discover original and novel ideas that lead to feasible alternative courses of action.

innovation The implementation of creative ideas in an organization.

- 1.** For organizational learning to occur, top managers must allow every person in the organization to develop a sense of personal mastery. Managers must empower employees and allow them to experiment and create and explore what they want.
- 2.** As part of attaining personal mastery, organizations need to encourage employees to develop and use *complex mental models*—sophisticated ways of thinking that challenge them to find new or better ways of performing a task—to deepen their understanding of what is involved in a particular activity. Here Senge is arguing that managers must encourage employees to develop a taste for experimenting and risk taking.⁷²
- 3.** Managers must do everything they can to promote group creativity. Senge thinks that *team learning* (learning that takes place in a group or team) is more important than individual learning in increasing organizational learning. He points out that most important decisions are made in subunits such as groups, functions, and divisions.
- 4.** Managers must emphasize the importance of *building a shared vision*—a common mental model that all organizational members use to frame problems or opportunities.
- 5.** Managers must encourage *systems thinking* (a concept drawn from systems theory). Senge emphasizes that to create a learning organization, managers must recognize the effects of one level of learning on another. Thus, for example, there is little point in creating teams to facilitate team learning if managers do not also take steps to give employees the freedom to develop a sense of personal mastery.

Building a learning organization requires that managers change their management assumptions radically. Developing a learning organization is neither a quick nor an easy process. Senge has been working with Ford Motor Company to help managers make Ford a learning organization. Why does Ford want this? Top management believes that to compete successfully, Ford must improve its members' ability to be creative and make the right decisions.

Increasingly, managers are being called on to promote global organizational learning. For example, managers at Wal-Mart use the lessons derived from its failures and successes in one country to promote global organizational learning across the many countries in which it now operates. For instance, when Wal-Mart entered Malaysia, it was convinced customers there would respond to its one-stop shopping format. It found, however, that Malaysians enjoy the social experience of shopping in a lively market or bazaar and thus did not like the impersonal efficiency of the typical Wal-Mart store. As a result, Wal-Mart has learned the importance of designing store layouts to appeal specifically to the customers of each country in which it operates.

When purchasing and operating a chain of stores in another country, such as the British ASDA chain, Wal-Mart now strives to retain what customers value in the local market while taking advantage of all of its own accumulated organizational learning. For example, Wal-Mart improved ASDA's information technology used for inventory and sales tracking in stores and enrolled ASDA in Wal-Mart's global purchasing operations, which has enabled the chain to pay less for certain products, sell them for less, and, overall, significantly increase sales. At the same time, Wal-Mart empowered local ASDA managers to run the stores; as the president of ASDA indicates, "This is still essentially a British business in the way it's run day to day."⁷³ Clearly, global organizational learning is essential for companies such as Wal-Mart that have significant operations in multiple countries.

Promoting individual creativity

Research suggests that when certain conditions are met, managers are more likely to be creative. As just discussed, people must be given the opportunity and freedom to generate new ideas. Creativity declines when managers look over the shoulders of talented employees and try to "hurry up" a creative solution. How would you feel if your boss said you had one week to come up with a new product idea to beat the competition? Creativity results when employees have an opportunity to experiment, to take risks, and to make mistakes and learn from them. And employees must not fear that they will be looked down on or penalized for ideas that might at first seem outlandish, as it is sometimes the ideas that initially seem outlandish that yield truly innovative products and services, as indicated in the following "Focus on Diversity."



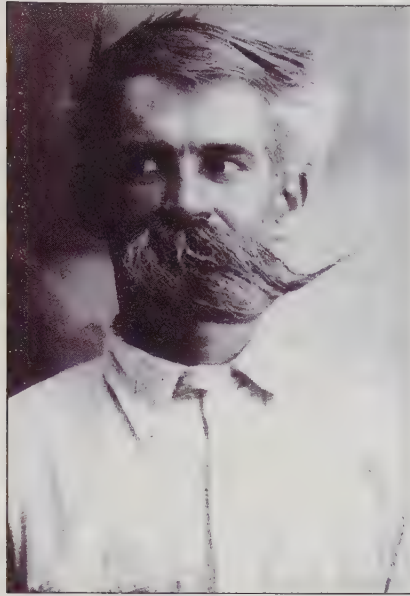
Focus on Diversity

Asking Different Questions and Providing Different Answers

Ideas for truly creative goods, products, and services sometimes come from asking different kinds of questions and seeking different kinds of answers. When George Ohr discovered the wonders of making clay pots at a potter's wheel in the late 1800s, he learned as much as he could about pots and then proceeded to question everything that people at the time thought pots should look like and provided answers in his own unique form of pottery art.⁷⁴

Disdained at the time, Ohr's pottery is now so revered for its creativity and beauty that his pots command five-digit prices and famed architect Frank Gehry is designing a museum (opening in 2006) in Ohr's hometown of Biloxi, Mississippi, to display Ohr's work.⁷⁵ Ohr turned pot making on its head. Each of his pots was unique: He would form perfect shapes and then crumple them like newspaper; he would make delicate, paper-thin pots; he carved writings into his pots; and he used bright, bold colors—all unheard of at the time and hailed as innovations decades later. It was only after Ohr's death that the art world recognized the genius and beauty in his work, which came from Ohr's unique answers to the question of pottery as an art form.⁷⁶

Asking the right questions and providing different kinds of answers can lead to creativity in other arenas as well.⁷⁷ Dr. William Hunter learned this from one of his professors in graduate school and has worked by it ever since.⁷⁸ Now, as



Creativity can sometimes seem initially outlandish. George Ohr turned pot making on its head in the early 1800s by questioning every pot-making norm of the time. Now his techniques are hailed as innovations.

about 20 percent of patients receiving them. The answer to this question is that stents used to open arteries can cause scar tissue to form around the stent, ultimately clogging the artery once again for certain patients. So why aren't stents coated with drugs that might help prevent the problem? Well, pharmaceutical companies have very long time horizons and spend large amounts of money on developing and testing new drugs. Medical equipment makers that develop and manufacture stents typically have much shorter time horizons. Hunter reasoned that paclitaxel, used in large dosages to stop the growth of cancer tumors, might prevent the growth of scar tissue when coated on stents in much smaller dosages.

After years of testing, Angiotech has a successful new product in paclitaxel-coated stents with only a 3 percent failure rate.⁸⁰ However, Hunter is the first to acknowledge that creative success and failure go hand in hand. For example, Angiotech unsuccessfully tried to develop a form of paclitaxel to treat multiple sclerosis. As Hunter puts it, "You have to celebrate the failures. . . . If you send the message that the only road to career success is experiments that work, people won't ask risky questions, or get any dramatically new answers."⁸¹ If he were alive today, George Ohr would likely concur.

CEO of Angiotech Pharmaceuticals in Vancouver, California, he encourages his employees to ask different kinds of questions and seek different answers. As a physician, he wondered whether drugs that were administered in massive doses to combat diseases like cancer could be used to cure or prevent other kinds of ailments when used in more moderate doses. And he also asked why medical implants like catheters and stents rarely included administrations of drugs. After extensive research, the answers to these questions led to the development of paclitaxel-coated coronary stents, a successful public offering of stock in Angiotech, and more questions for future research.⁷⁹

Hunter learned that stents were not coated with drugs because of the questions stent manufacturers asked physicians. Typically, they would ask surgeons for advice on how to make better stents. Hunter, on the other hand, asked surgeons why stents sometimes fail and cause problems for

Highly innovative companies like 3M are well known for the wide degree of freedom they give their managers and employees to ask different questions and seek their answers. For example, at 3M employees are expected to spend a certain percentage of their time on projects of their own choosing, a policy that fosters creativity.

Once managers have generated alternatives, creativity can be fostered by providing them with constructive feedback so that they know how well they are doing.

Ideas that seem to be going nowhere can be eliminated and creative energies refocused in other directions. Ideas that seem promising can be promoted, and help from other managers can be obtained as well.⁸²

Top managers must also stress the importance of looking for alternative solutions and should visibly reward employees who come up with creative ideas. Being creative can be demanding and stressful. Employees who believe that they are working on important, vital issues are motivated to put forth the high levels of effort that creativity demands. Creative people like to receive the acclaim of others, and innovative organizations have many kinds of ceremonies and rewards to recognize creative employees. For example, 3M established the Carlton Hall of Fame to recognize successful innovators. These employees not only become members of the hall of fame but also receive financial rewards through the Golden Step program.

Promoting group creativity

To encourage creativity at the group level, organizations can make use of group problem-solving techniques that promote creative ideas and innovative solutions. These techniques can also be used to prevent groupthink and to help managers uncover biases. Here, we look at three group decision-making techniques: brainstorming, the nominal group technique, and the Delphi technique.

BRAINSTORMING *Brainstorming* is a group problem-solving technique in which managers meet face-to-face to generate and debate a wide variety of alternatives from which to make a decision.⁸³ Generally, from 5 to 15 managers meet in a closed-door session and proceed like this:

1. One manager describes in broad outline the problem the group is to address.
2. Group members then share their ideas and generate alternative courses of action.
3. As each alternative is described, group members are not allowed to criticize it; everyone withholds judgment until all alternatives have been heard. One member of the group records the alternatives on a flip chart.
4. Group members are encouraged to be as innovative and radical as possible. Anything goes; and the greater the number of ideas put forth, the better. Moreover, group members are encouraged to “piggyback” or build on each other’s suggestions.
5. When all alternatives have been generated, group members debate the pros and cons of each and develop a short list of the best alternatives.

Brainstorming is very useful in some problem-solving situations—for example, when managers are trying to find a new name for a perfume or for a model of car. But sometimes individuals working alone can generate more alternatives. The main reason for the loss of productivity in brainstorming appears to be **production blocking**, which occurs because group members cannot always simultaneously make sense of all the alternatives being generated, think up additional alternatives, and remember what they were thinking.⁸⁴

NOMINAL GROUP TECHNIQUE To avoid production blocking, the **nominal group technique** is often used. It provides a more structured way of generating alternatives in writing and gives each manager more time and opportunity to come up with potential solutions. The nominal group technique is especially useful when

production blocking A loss of productivity in brainstorming sessions due to the unstructured nature of brainstorming.

nominal group technique A decision-making technique in which group members write down ideas and solutions, read their suggestions to the whole group, and discuss and then rank the alternatives.

an issue is controversial and when different managers might be expected to champion different courses of action. Generally, a small group of managers meet in a closed-door session and adopt the following procedures:

- One manager outlines the problem to be addressed, and 30 or 40 minutes are allocated for group members, working individually, to write down their ideas and solutions. Group members are encouraged to be innovative.
- Managers take turns reading their suggestions to the group. One manager writes all the alternatives on a flip chart. No criticism or evaluation of alternatives is allowed until all alternatives have been read.
- The alternatives are then discussed, one by one, in the sequence in which they were first proposed. Group members can ask for clarifying information and critique each alternative to identify its pros and cons.
- When all alternatives have been discussed, each group member ranks all the alternatives from most preferred to least preferred, and the alternative that receives the highest ranking is chosen.⁸⁵

DELPHI TECHNIQUE Both the nominal group technique and brainstorming require that managers meet together to generate creative ideas and engage in joint problem solving. What happens if managers are in different cities or in different parts of the world and cannot meet face-to-face? Videoconferencing is one way to bring distant managers together to brainstorm. Another way is to use the **Delphi technique**, a written approach to creative problem solving.⁸⁶ The Delphi technique works like this:

- The group leader writes a statement of the problem and a series of questions to which participating managers are to respond.
- The questionnaire is sent to the managers and departmental experts who are most knowledgeable about the problem. They are asked to generate solutions and mail the questionnaire back to the group leader.
- A team of top managers records and summarizes the responses. The results are then sent back to the participants, with additional questions to be answered before a decision can be made.
- The process is repeated until a consensus is reached and the most suitable course of action is apparent.

delphi technique

A decision-making technique in which group members do not meet face-to-face but respond in writing to questions posed by the group leader.

Promoting creativity at the global level

The Delphi technique is particularly useful when barriers of time and distance, a situation that is common in the global environment, separate managers. Today, organizations are under increasing pressure to reduce costs and develop global products. To do so, they typically centralize their research and development expertise by bringing R&D managers together at one location. Encouraging creativity among teams of R&D experts from different countries poses special problems, however. First, R&D experts often have difficulty communicating their ideas to one another because of language problems and because of cultural differences in their approaches to problem solving. Second, the decision-making process differs from country to country. In Japan, for example, decisions tend to be made in a very participative manner, and the group as a whole must agree on a course of action before a decision is made. In contrast, decision making is very centralized in Mexico; top managers decide what to do, with little input from subordinates.

Managers must take special steps to encourage creativity among people from different countries who are supposed to be working together. They must develop training programs that promote awareness and understanding so that diverse individuals can cooperate and brainstorm new ideas and approaches to problems, opportunities, and threats.

Summary and Review

THE NATURE OF MANAGERIAL DECISION MAKING

Programmed decisions are routine decisions made so often that managers have developed decision rules to be followed automatically. Nonprogrammed decisions are made in response to situations that are unusual or novel; they are non-routine decisions. The classical model of decision making assumes that decision makers have complete information; are able to process that information in an objective, rational manner; and make optimum decisions. March and Simon argue that managers are boundedly rational, rarely have access to all the information they need to make optimum decisions, and consequently satisfice and rely on their intuition and judgment when making decisions.

STEPS IN THE DECISION-MAKING PROCESS When making decisions, managers should take these six steps: Recognize the need for a decision, generate alternatives, assess alternatives, choose among alternatives, implement the chosen alternative, and learn from feedback.

GROUP DECISION MAKING Many advantages are associated with group decision making, but there are also several disadvantages. One major source of poor decision making is groupthink. Afflicted decision makers collectively embark on a dubious course of action without questioning the assumptions that underlie their decision. Managers can improve the quality of group decision making by using techniques such as devil's advocacy and by increasing diversity in the decision-making group.

ORGANIZATIONAL LEARNING AND CREATIVITY Organizational learning is the process through which managers seek to improve employees' desire and ability to understand and manage the organization and its task environment so that employees can make decisions that continuously raise organizational effectiveness. Managers must take steps to promote organizational learning and creativity at the individual and group levels to improve the quality of decision making.



Management in Action

Topics for Discussion and Action

Discussion

1. What are the main differences between programmed decision making and nonprogrammed decision making?
2. In what ways do the classical and administrative models of decision making help managers appreciate the complexities of real-world decision making?
3. Why do capable managers sometimes make bad decisions? What can individual

managers do to improve their decision-making skills?

4. In what kinds of groups is groupthink most likely to be a problem? When is it least likely to be a problem? What steps can group members take to ward off groupthink?
5. What is organizational learning, and how can managers promote it?

Action

6. Ask a manager to recall the best and the worst decisions

he or she ever made. Try to determine why these decisions were so good or so bad.

7. Think about an organization in your local community, your university, or an organization that you are familiar with that is doing poorly. Now come up with questions managers in this organization should ask stakeholders to elicit creative ideas for turning around the organization's fortunes.



Building Management Skills

How Do You Make Decisions?

Pick a decision that you made recently and that has had important consequences for you. It may be your decision about which college to attend, which major to select, whether to take a part-time job, or which part-time job to take. Using the material in this chapter, analyze the way in which you made the decision—in particular:

1. Identify the criteria you used, either consciously or unconsciously, to guide your decision making.
2. List the alternatives you considered. Were they all possible alternatives? Did you unconsciously (or consciously) ignore some important alternatives?
3. How much information did you have about each alternative?

Were you making the decision on the basis of complete or incomplete information?

4. Try to remember how you reached the decision. Did you sit down and consciously think through the implications of each alternative, or did you make the decision on the basis of intuition? Did you use any rules of thumb to help you make the decision?

5. In retrospect, do you think that your choice or alternative was shaped by any of the cognitive biases discussed in this chapter?
6. Having answered the previous five questions, do you think in retrospect that you made a reasonable decision? What, if anything, might you do to improve your ability to make good decisions in the future?





Small Group Breakout Exercise

Brainstorming

Form groups of three or four people, and appoint one member as the spokesperson who will communicate your findings to the whole class when called on by the instructor. Then discuss the following scenario.

You and your partners are trying to decide which kind of restaurant to open in a centrally located shopping center that has just been built in your city. The problem confronting you is that the city already has many restaurants that provide different kinds of food in all price ranges. You have the resources to open any type of restaurant. Your challenge is to decide which type is most likely to succeed.

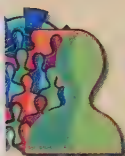
Use the brainstorming technique to decide which type of restaurant to open. Follow these steps:

1. As a group, spend 5 or 10 minutes generating ideas about the alternative restaurants that the members think will be most likely to succeed. Each group member should be as innovative and creative as possible, and no suggestions should be criticized.
2. Appoint one group member to write down the alternatives as they are identified.
3. Spend the next 10 or 15 minutes debating the pros and

cons of the alternatives. As a group, try to reach a consensus on which alternative is most likely to succeed.

After making your decision, discuss the pros and cons of the brainstorming method, and decide whether any production blocking occurred.

When called on by the instructor, the spokesperson should be prepared to share your group's decision with the class, as well as why the group made its decision.



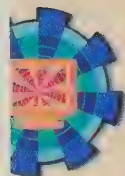
Be the Manager

You are a top manager who was recently hired by an oil field services company in Oklahoma to help it respond more quickly and proactively to potential opportunities in its market. You report to the chief operating officer (COO), who reports to the CEO, and you have been on the job for eight months. Thus far, you have come up with three initiatives you carefully studied, thought were noteworthy, and proposed and justified to the COO. The COO seemed cautiously interested when you presented the proposals, and each time he indicated he would think about them and discuss them with the CEO as con-

siderable resources were involved. Each time, you never heard back from the COO, and after a few weeks elapsed, you casually asked the COO if there was any news on the proposal in question. For the first proposal, the COO said, "We think it's a good idea but the timing is off. Let's shelve it for the time being and reconsider it next year." For the second proposal, the COO said, "Mike [the CEO] reminded me that we tried that two years ago and it wasn't well received in the market. I am surprised I didn't remember it myself when you first described the proposal, but it came right back to me once Mike mentioned it." For the

third proposal, the COO simply said, "We're not convinced it will work."

You believe that your three proposed initiatives are viable ways to seize opportunities in the marketplace, yet you cannot proceed with any of them. Moreover, for each proposal, you invested considerable amounts of time and even worked to bring others on board to support the proposal, only to have it shot down by the CEO. When you interviewed for the position, both the COO and the CEO claimed they wanted "an outsider to help them step out of the box and innovate." Yet your experience to date has been just the opposite. What are you going to do?



Additional Activities on the Build Your Management Skills DVD

- **Test Your Knowledge:** The Vroom/Yetton/Jago Decision Model
- **Self-Assessment:** (1) Your Preferred Decision-Making Style and (2) Assessing Your Creativity Quotient
- **Manager's Hot Seat:** (2) Whistleblowing: Code Red or Red Ink

Managing Ethically

Sometimes groups make extreme decisions—decisions that are either more risky or more conservative than they would have been if individuals acting alone had made them. One explanation for the tendency of groups to make extreme decisions is diffusion of responsibility. In a group, responsibility for the outcomes of a decision

is spread among group members, so each person feels less than fully accountable. The group's decision is extreme because no individual has taken full responsibility for it.

Questions

1. Either alone or in a group, think about the ethical

implications of extreme decision making by groups.

2. When group decision making takes place, should members of the group each feel fully accountable for outcomes of the decision? Why or why not?



Case for Discussion

By all counts, Tadataka (Tachi) Yamada faced a challenging task. Yamada was a top manager at SmithKline Beecham, one of the world's largest pharmaceutical companies, when things couldn't seem more dismal.⁸⁷ Not enough potential drugs were in the pipeline, patents on top-selling drugs like Paxil were nearing their expiration dates, and SmithKline Beecham was in the process of merging with Glaxo Wellcome, a pharmaceutical company with similar challenges.⁸⁸ Yamada's task was no less than daunting—reinvent the 15,000-people-strong R&D function of the merged company, GlaxoSmithKline, to fill the company's pipeline with promising new drugs. As Jean-Pierre Garnier, the new CEO of the just merged company, put it, "We can't keep doing what we're doing. . . . So start thinking about something radical."⁸⁹

Yamada was up for the challenge and made bold decisions to reinvent R&D at GlaxoSmithKline (Glaxo). Interestingly, his efforts focused on changing the way decisions were traditionally made in the company. This was not an easy process—it took three years, the support and commitment of Garnier, and the courage of Yamada. It was rough going during much of this period, but by 2004 Yamada's reorientation of

decision making started paying off. While only a few new drugs were under development in 2001, by 2004 Glaxo had over 40 drugs in phases 2 and 3 of clinical trials.⁹⁰ And in 2005, Glaxo had over 190 vaccine and pharmaceutical projects under development.⁹¹

What did Yamada decide that changed the fate of Glaxo? Taking a bold step, he decided not to do what typically is done after such a megamerger—consolidate R&D across the newly merged companies, lay off employees, and focus on cutting costs. Rather, Yamada went back to his research roots (he has an MD degree and was formerly the chairman of the Internal Medicine Department at the University of Michigan Medical School).⁹² He decided that to develop new drugs, R&D employees need to think and act like entrepreneurs—making decisions that they believe in and being highly motivated to follow through to make them a success.⁹³

Yamada restructured R&D at Glaxo by forming autonomous, entrepreneurial start-up labs to develop new drugs. Rather than consolidating decision making at the top, which usually happens after a merger, he empowered researchers in the labs to make the decisions that would hopefully revive Glaxo or seal its fate. Yamada's bold experiment was a tes-

tament to his belief that the research scientists responsible for discovering and developing new drugs should be making the key decisions—not top executives, who are a step removed from the research process on a day-to-day basis. Given the huge investments and lengthy time horizons involved—developing a new drug and getting it approved by the U.S. Food and Drug Administration (FDA) typically takes about 10 years and costs about \$800 million—giving research scientists the final say on what new drugs to pursue was a dramatic departure from the tradition of having top managers make such decisions.⁹⁴

Yamada divided R&D at Glaxo into six small, semiautonomous labs, each with a primary research focus, such as cardiovascular disease or cancer. Rather than operating as R&D typically does in a large company, these labs resemble biotech start-ups: Each has its own top managers, budget, and staff (kept deliberately small, at no more than 400 employees). Not only do the labs decide what drugs to pursue, but they also follow through with their decisions into the clinical testing phase. Previously, as is typical in large pharmaceutical companies, once R&D discovered new drugs, it passed them on to other units responsible for getting the drugs into clinical testing.



Yamada wanted the researchers who were closest to the new discoveries to take ownership of them, make key decisions on how to proceed, and be responsible for their success (or failure). Importantly, researchers are rewarded for their expanded role in drug development; those who succeed at discovering a new drug and moving it into clinical testing are rewarded with bonuses and royalties.⁹⁵

This restructuring of R&D was a major change from the status quo at Glaxo, a change that during the first two years seemed doomed to failure. Setting up the new lab structure, redesigning jobs, dismantling the decision-making hierarchy, and empowering scientists to make key decisions resulted in turf battles, chaos, and high levels of uncertainty and stress. Many R&D scientists and executives fled the chaos to work for other companies, and

the price of Glaxo shares declined by almost 20 percent.⁹⁶

Garnier and Yamada believed in what they were doing and were willing to carry on making tough decisions to make it a success. While the ultimate outcome of their bold decisions will take years to crystallize in terms of FDA-approved, effective new drugs for treating diseases, things are now looking bright at Glaxo. In 2003, Glaxo approximately doubled over 2001 the number of new drugs it was advancing into Phase I and II trials, and accelerated earlier-stage discovery efforts with new automated drug-screening facilities.⁹⁷ Yamada's willingness to take risks to enhance long-term viability, innovation, and success seems to be paying off at Glaxo. It has convinced many, including Allen Oliff, a top research executive recruited from Merck to head a new cancer lab,⁹⁸

that Yamada has successfully reinvented R&D at Glaxo. The wisdom of his efforts has not gone unnoticed at the very highest levels of the company. In 2004, the 58-year-old Yamada was named executive director/chairman of research and development and became a member of Glaxo's board of directors.⁹⁹

Questions

1. How did the way in which Yamada's restructured R&D change the decision-making process?
2. Why did some employees leave the company while these changes were taking place?
3. Why did Yamada make the changes he did?
4. Why is it important for R&D employees to think and to make decisions like entrepreneurs?

BusinessWeek

Case in the News

The Brains Behind BlackBerry

They are the odd couple of the wireless world. One is a Turkish-born whiz kid who grew up across the border from Detroit and later dropped out of college to build an industrial display network for General Motors Corp.; the other, an ambitious tradesman's son from rural Ontario who glided through one of Canada's top colleges and Harvard Business School before settling into corporate life. But as co-chief executives of Research in Motion Ltd. (RIM), Mike Lazaridis and Jim Balsillie, both 43, are the quiet men behind the hottest wireless email gadget around: the BlackBerry. Among the million-plus subscribers are such reported fans as Jeb Bush, Bill Gates, Sarah Jessica Parker, and Jack Welch. From the near-constant clicking in the halls of Congress to its spot on Oprah Winfrey's "favorite

things of 2003" list, the BlackBerry has become almost shorthand for wireless email itself.

The addictive little devices, introduced in early 1999, defy many of the stereotypes of high tech. They were spawned far from Silicon Valley in Waterloo, Ont., a quiet university town of 99,000 about an hour's drive west of Toronto. And RIM is no glitzy startup; Lazaridis founded it two decades ago to consult and develop technologies like the film bar-code readers that would eventually win him a technical Emmy and an Oscar.

Still, nothing has ever rocked RIM and its hometown like the BlackBerry. The brand has become the industry standard, far better known than its cryptically named parent, and a cultural icon to boot. Every major carrier wants to offer it to its customers. Everyone wants to

work there. And that stock price! It has roared from \$12.75 to \$108 over the past year, and on April 7 the company announced a two-for-one split. Lazaridis' stake is worth \$782 million, while Balsillie's comes to \$674 million. Even so, Balsillie has banned staff from checking the price at the office.

Instead, the co-CEOs have obsessed over the core product: email that is automatically pushed to the BlackBerry as it's going to the desktop and can be instantly answered with an intuitive, thumb-operated keyboard. Notes Andy Brown, chief technology architect at Merrill Lynch & Co.: "People don't want wireless email. They want a BlackBerry." But that may not always be so. The duo have forged deals with companies ranging from Microsoft Corp. to Palm-Source Inc. to license BlackBerry

software. Think “Intel Inside.” And they recently signed a deal with Sun Microsystems Inc. to extend wireless Web services to BlackBerry customers. The goal, says Balsillie, is “to enable wireless email whenever and on whatever device people want.”

But RIM’s quirky duo are hardly alone in their passion for wireless e-mail. They face competition ranging from pocket PC devices to similar handhelds put out by Good Technology Inc., which just settled a patent lawsuit with RIM and agreed to pay royalties for using its technology. And they have their own legal battles with Virginia’s NTP Inc., which alleges RIM and numerous other wireless email operators infringed its 1990 patents. RIM lost the first round in court; the case is on appeal.

“Science is the Core”

Still, the company’s main challenge at the moment may be gearing up for explosive growth. With added features like voice, color screens, and international roaming, analysts predict that the number of customers could easily double this year, to 2 million. On April 7, RIM said its subscriber base increased by 24 percent, to almost 1.1 million, in the fourth quarter ended February 28. It also reported sales of \$210.6 million, up 37 percent from the previous quarter, while profits rose 255 percent, to \$41.5 million.

Those who know RIM attribute much of its success to the complementary relationship of its co-CEOs. Without Lazaridis, the silver-haired science buff who once won a special award from his public school for checking every science and math book out of the library, RIM would have no technology. “Science is the core of everything, yet we take it for granted,” he says. And without Balsillie, the business maven who as a young father mortgaged his house

and poured much of his net worth into Lazaridis’ fledgling operation in 1992, it would have far less commercial success. As he puts it, “People capitalize on opportunities. They don’t create them.” He is the corporate strategist, the financial wizard, the negotiator, and the face of the company on Wall Street. Lazaridis is the science mastermind, the production guru, the dreamer, and the one who solves customers’ problems. He likes to frequent physics lectures and read books like *Sojourner: An Insider’s View of the Mars Pathfinder Mission*. But his real hobby is, well, thinking about RIM. Balsillie coaches his son’s basketball team, races into Toronto for Maple Leafs hockey games, and cherishes time in his cottage on Georgian Bay.

Despite such obvious differences, though, the two men share some important similarities. First is their conviction, stretching back a decade, that people would one day want constant access to email through a device they could hook on their belts. Balsillie, who joined the then-tiny outfit when Lazaridis wooed him from a customer to manage the business in 1992, calls email “one of the most profound medium shifts we’ll ever see.” Lazaridis never doubted it for a minute. Even now, he gets visibly exasperated when RIM is treated like some kind of here-today-gone-tomorrow dot-com. “We’ve passed all the initiation by fire to get to 20 years old,” he says, noting that RIM went public five years ago and now has a market capitalization of almost \$10 billion.

They are equally relentless about pushing the BlackBerry. In 1999, they were so sure that it would just take a few days with one to get hooked that they hired “evangelists” to lend the devices out to executives on Wall Street. That helped the no-name Canadian company win contracts with a number of big firms. “You immediately saw

everyone get it,” recalls Leonard G. Rosen, a technology banker and managing director at Lehman Brothers Inc., which works with RIM. Soon, the company decided to let the network carriers offer BlackBerries to their customers. The pay-off for RIM is clear: 65 percent plus margins on the service and 35 percent plus margins on the hardware, according to analyst Deepak Chopra of National Bank Financial.

Both men are building a legacy beyond the BlackBerry. Lazaridis donated about \$100 million (Canadian) in stock to start Waterloo’s Perimeter Institute for Theoretical Physics in 2000, while Balsillie gave \$30 million to start the Centre for International Governance Innovation two years later. But they’re nowhere near retirement. Defending RIM’s niche will take all of Balsillie’s strategic smarts. This odd couple is smack in the middle of the hot zone.

Questions

1. What factors are responsible for the success of BlackBerry?
2. What are Lazaridis’s and Balsillie’s distinctive qualities as top managers and decision makers?
3. Up to this point, these two top managers at RIM have seemed to make good decisions. Why do you think they have been successful?
4. Looking to the future, what challenges will RIM, BlackBerry, and Lazaridis and Balsillie face? Do you think these co-CEOs are up for the challenge and will continue to make decisions that contribute to the success of RIM and BlackBerry? Why or why not?

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CHAPTER

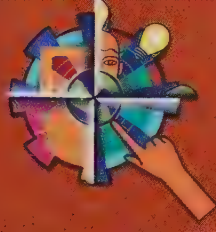
6

Planning, Strategy, and Competitive Advantage

Learning Objectives

After studying this chapter, you should be able to:

- Describe the three steps of the planning process and the relationship between planning and strategy.
- Explain the role of planning in predicting the future and in mobilizing organizational resources to meet future contingencies.
- Outline the main steps in SWOT analysis.
- Differentiate among corporate-, business-, and functional-level strategies.
- Describe the vital role played by strategy implementation in determining managers' ability to achieve an organization's mission and goals.



Management Snapshot

Chris McCormick's New Strategy for L. L. Bean

What is the best way to compete in an industry?

In 1911 Leon Leonwood Bean, a hunter, grew weary of walking miles with wet feet in search of game and so he decided to invent a waterproof boot with leather uppers attached to a large rounded rubber base and sole. Soon, Bean began selling his boots through mail order. As word spread about the boot's reliability and backed by his policy of being responsive to customers who complained—often replacing their boots years after a sale—L. L. Bean's reputation spread. As the years went by the company expanded its now well-known product line to include canvas tote bags and flannel dog beds. By 2000 the company's mail order revenues exceeded \$1 billion a year. Bean became known for offering one of the broadest and highest-quality product lines of sporting clothes and accessories available.

The company built a 160,000 square foot signature store in Freeport, Maine, to display its product line. The store stocks hundreds of versions of L. L. Bean back packs, fleece

vests, shirts, moccasins, tents, and so forth. Over three million visitors a year shop this signature store. One reason for establishing the store was to give customers hands-on access to the high-quality L. L. Bean products. Of course, Bean expected to command



a premium price for offering a wide variety of high-quality products, and historically the store has enjoyed high profit margins.

Bean's business began to suffer in the mid-1990s, however, when a number of other companies began offering similar high-quality, high-priced products to customers, and Bean's catalogue lost its unique appeal. Furthermore, the growth of the Internet throughout the

1990s gave customers access to many more specialized companies offering quality products, often at much lower prices. For example, Lands' End also began to feature fleece vests, dog baskets, and so on. The problem facing any company offering unique, high-end products is that competitors will try to copy or imitate the products and then offer customers similar kinds of products at lower prices.

Finding ways to protect and increase the company's business has proved to be a major challenge for Bean. Chris McCormick, the current CEO, is trying to craft new strategies to help Bean rebuild its competitive advantage.¹ Among these strategies is to build a chain of L. L. Bean stores in major urban locations to attract more customers and showcase the quality of products so customers either buy the products at the store or purchase them from the L. L. Bean Web site. McCormick hopes to have ten stores open by

2010 but this is not proving easy because bricks and mortar retail stores are expensive to run. Bean also has had to lower the prices of its sports clothing and accessories in these stores because competition means it can no longer charge the premium prices.

Another strategy has been to launch an aggressive advertising campaign aimed at younger customers who may not know the Bean story. Then with the physical stores, the Internet, and the catalogues L. L. Bean may have a better chance of obtaining their business.

The jury is out on whether McCormick can turn around Bean's performance. Not only are other differentiated sporting goods chains, such as Dick's Sporting Goods and Gander Mountain, expanding, but Web sites such as Amazon.com and Lands' End are offering similar products at lower prices.

Overview

As the opening case suggests, there is more than one way for a company to compete in an industry, and to compete effectively,

a company's managers must study the way other organizations operate and identify their strategies. By studying how L. L. Bean's competitors have been imitating its products and then selling them in new kinds of bricks and mortar stores and virtual stores, Chris McCormick is devising strategies that he hopes will allow Bean to fight back and prosper in the years ahead.

In an uncertain competitive environment, managers must engage in thorough planning to find a strategy that will allow them to compete effectively. This chapter explores the manager's role both as planner and as strategist. We discuss the different elements involved in the planning process, including its three major steps: (1) determining an organization's mission and major goals, (2) choosing strategies to realize the mission and goals, and (3) selecting the appropriate way of organizing resources to implement the strategies. We also discuss scenario planning and SWOT analysis, important techniques that managers use to analyze their current situation. By the end of this chapter, you will understand the role managers play in the planning and strategy-making process to create high-performing organizations.

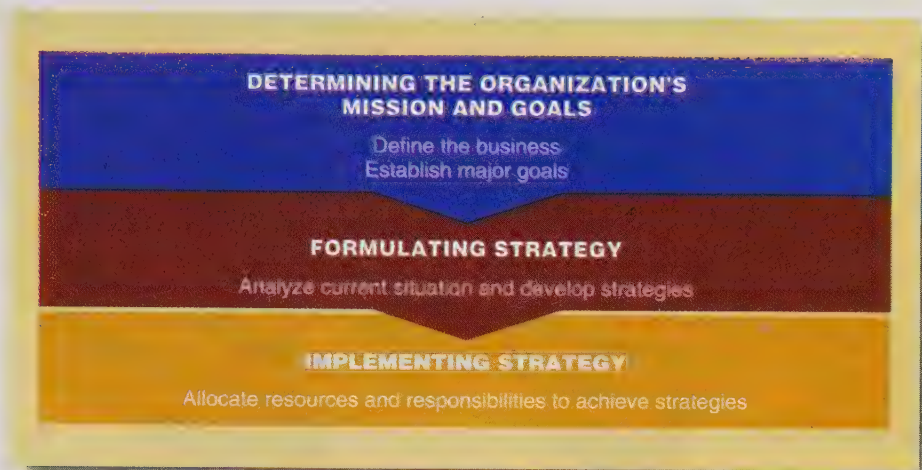
planning Identifying and selecting appropriate goals and courses of action; one of the four principal functions of management.

strategy A cluster of decisions about what goals to pursue, what actions to take, and how to use resources to achieve goals.

The Nature of the Planning Process

Planning, as we noted in Chapter 1, is a process that managers use to identify and select appropriate goals and courses of action for an organization.² The organizational plan that results from the planning process details the goals of the organization and specifies how managers intend to attain those goals. The cluster of decisions and actions that

managers take to help an organization attain its goals is its **strategy**. Thus, planning is both a goal-making and a strategy-making process.

Figure 6.1**Three Steps in Planning****mission statement**

A broad declaration of an organization's purpose that identifies the organization's products and customers and distinguishes the organization from its competitors.

In most organizations, planning is a three-step activity (see Figure 6.1). The first step is determining the organization's mission and goals. A **mission statement** is a broad declaration of an organization's overriding purpose; this statement is intended to identify an organization's products and customers as well as to distinguish the organization in some way from its competitors. The second step is formulating strategy. Managers analyze the organization's current situation and then conceive and develop the strategies necessary to attain the organization's mission and goals. The third step is implementing strategy. Managers decide how to allocate the resources and responsibilities required to implement the strategies between people and groups within the organization.³ In subsequent sections of this chapter we look in detail at the specifics of each of these steps. But first we examine the general nature and purpose of planning, one of the four managerial functions identified by Henri Fayol.

Levels of planning

division A business unit that has its own set of managers and functions or departments and competes in a distinct industry.

divisional managers Managers who control the various divisions of an organization.

corporate-level plan Top management's decisions pertaining to the organization's mission, overall strategy, and structure.

In large organizations planning usually takes place at three levels of management: corporate, business or division, and department or functional. Figure 6.2 shows the link between the three steps in the planning process and these three levels. To understand this model, consider how General Electric (GE), a large organization that competes in many different businesses, operates.⁴ GE has three main levels of management: corporate level, business level, and functional level (see Figure 6.3). At the corporate level are CEO and Chairman Jeffrey Immelt, three other top managers, and their corporate support staff. Below the corporate level is the business level. At the business level are the different divisions of the company. A **division** is a business unit that competes in a distinct industry; GE has over 150 divisions, including GE Aircraft Engines, GE Financial Services, GE Lighting, GE Motors, GE Plastics, and NBC. Each division has its own set of **divisional managers**. In turn, each division has its own set of functions or departments—manufacturing, marketing, human resource management, R&D, and so on. Thus, GE Aircraft has its own marketing function, as do GE Lighting, GE Motors, and NBC.

At GE, as at other large organizations, planning takes place at each level. The **corporate-level plan** contains top management's decisions pertaining to the

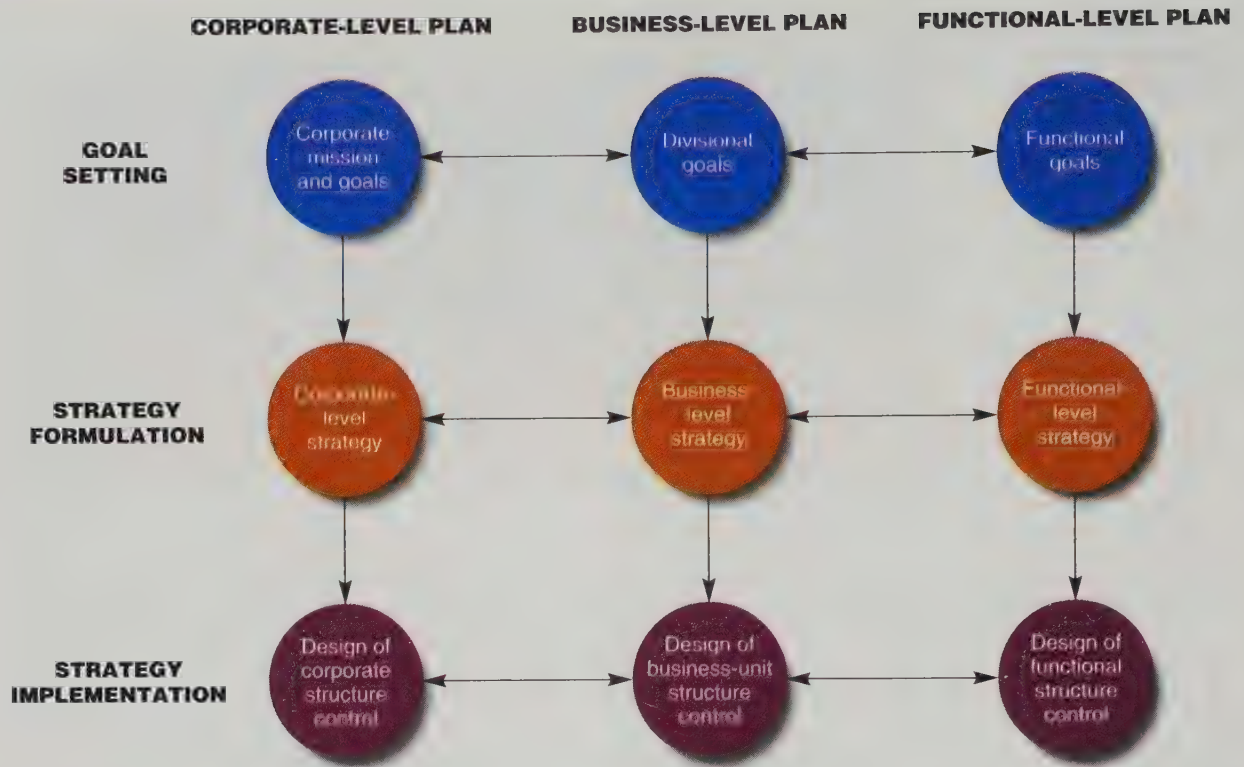


Figure 6.2
Levels and Types of Planning

corporate-level strategy A plan that indicates in which industries and national markets an organization intends to compete.

business-level plan Divisional managers' decisions pertaining to divisions' long-term goals, overall strategy, and structure.

business-level strategy A plan that indicates how a division intends to compete against its rivals in an industry.

organization's mission and goals, overall (corporate-level) strategy, and structure (see Figure 6.2). **Corporate-level strategy** indicates in which industries and national markets an organization intends to compete. One of the goals stated in GE's corporate-level plan is that GE should be first or second in market share in every industry in which it competes. A division that cannot attain this goal may be sold to another company. GE Medical Systems was sold to Thompson of France for this reason. Another GE goal is the acquisition of other companies to help build market share. Over the last decade, GE has acquired several financial services companies and has transformed the GE Financial Services Division into one of the largest financial services operations in the world.

The corporate-level plan provides the framework within which divisional managers create their business-level plans. At the business level, the managers of each division create a **business-level plan** that details (1) long-term goals that will allow the division to meet corporate goals and (2) the division's business-level strategy and structure. **Business-level strategy** states the methods a division or business intends to use to compete against its rivals in an industry. Managers at GE Lighting (currently number two in the global lighting industry, behind the Dutch company Philips NV) develop strategies designed to help the division take over the number-one spot and better contribute to GE's corporate goals. The lighting division's competitive strategy might emphasize, for example, trying to reduce costs in all

Figure 6.3
Levels of
Planning at
General Electric



function A unit or department in which people have the same skills or use the same resources to perform their jobs.

functional managers Managers who supervise the various functions, such as manufacturing, accounting, and sales, within a division.

functional-level plan Functional managers' decisions pertaining to the goals that they propose to pursue to help the division attain its business-level goals.

functional-level strategy A plan that indicates how a function intends to achieve its goals.

departments in order to lower prices and gain market share from Philips. GE is currently planning to expand its European lighting operations, which, as we discussed in Chapter 6, is based in Hungary.⁵

A **function** is a unit or department in which people have the same skills or use the same resources to perform their jobs. Examples include manufacturing, accounting, and sales. The business-level plan provides the framework within which **functional managers** devise their plans. A **functional-level plan** states the goals that functional managers propose to pursue to help the division attain its business-level goals, which, in turn, allow the organization to achieve its corporate goals. **Functional-level strategy** sets forth the actions that managers intend to take at the level of departments such as manufacturing, marketing, and R&D to allow the organization to attain its goals. Thus, for example, consistent with GE Lighting's strategy of driving down costs, the manufacturing function might adopt the goal "To reduce production costs by 20 percent over three years," and its functional strategy to achieve this goal might include (1) investing in state-of-the-art European production facilities and (2) developing an electronic global business-to-business network to reduce the costs of inputs and inventory holding.

An important issue in planning is ensuring consistency in planning across the three different levels. Functional goals and strategies should be consistent with divisional goals and strategies, which in turn should be consistent with corporate goals and strategies, and vice versa. Once complete, each function's plan is normally linked to its division's business-level plan, which, in turn, is linked to the corporate plan. Although few organizations are as large and complex as GE, most plan as GE does and have written plans to guide managerial decision making.

Who plans?

In general, corporate-level planning is the primary responsibility of top managers.⁶ At General Electric, the corporate-level goal that GE be first or second in every industry in which it competes was first articulated by former CEO Jack Welch. Now, Welch's hand-selected successor, Jeffrey Immelt, and his top-management team decide which industries GE should compete in. Corporate-level managers are responsible for approving business- and functional-level plans to ensure that they are consistent with the corporate plan.

Corporate planning decisions are not made in a vacuum. Other managers do have input to corporate-level planning. At General Electric and many other companies, divisional and functional managers are encouraged to submit proposals for new business ventures to the CEO and top managers, who evaluate the proposals and decide whether to fund them.⁷ Thus, even though corporate-level planning is the responsibility of top managers, lower-level managers can and usually are given the opportunity to become involved in the process.

This approach is common not only at the corporate level but also at the business and functional levels. At the business level, planning is the responsibility of divisional managers, who also review functional plans. Functional managers also typically participate in business-level planning. Similarly, although the functional managers bear primary responsibility for functional-level planning, they can and do involve their subordinates in this process. Thus, although ultimate responsibility for planning may lie with certain select managers within an organization, all managers and many nonmanagerial employees typically participate in the planning process.

Time horizons of plans

time horizon The intended duration of a plan.

Plans differ in their **time horizons**, or intended durations. Managers usually distinguish among *long-term plans*, with a horizon of five years or more; intermediate-term plans, with a horizon between one and five years; and *short-term plans*, with a horizon of one year or less.⁸ Typically, corporate- and business-level goals and strategies require long- and intermediate-term plans, and functional-level goals and strategies require intermediate- and short-term plans.

Although most organizations operate with planning horizons of five years or more, it would be inaccurate to infer from this that they undertake major planning exercises only once every five years and then “lock in” a specific set of goals and strategies for that time period. Most organizations have an annual planning cycle, which is usually linked to the annual financial budget (although a major planning effort may be undertaken only every few years).

Although a corporate- or business-level plan may extend over five years or more, it is typically treated as a *rolling plan*, a plan that is updated and amended every year to take account of changing conditions in the external environment. Thus, the time horizon for an organization's 2005 corporate-level plan might be 2010; for the 2006 plan it might be 2011; and so on. The use of rolling plans is essential because of the high rate of change in the environment and the difficulty of predicting competitive conditions five years in the future. Rolling plans allow managers to make midcourse corrections if environmental changes warrant or to change the thrust of the plan altogether if it no longer seems appropriate. The use of rolling plans allows managers to plan flexibly, without losing sight of the need to plan for the long term.

Standing plans and single-use plans

Another distinction often made between plans is whether they are standing plans or single-use plans. Managers create standing and single-use plans to help achieve an organization's specific goals. *Standing plans* are used in situations in which programmed decision making is appropriate. When the same situations occur repeatedly, managers develop policies, rules, and standard operating procedures (SOPs) to control the way employees perform their tasks. A *policy* is a general guide to action; a *rule* is a formal, written guide to action; and a *standing operating procedure* is a written instruction describing the exact series of actions that should be followed in a specific situation. For example, an organization may have a standing plan about ethical behavior by employees. This plan includes a policy that all employees are expected to behave ethically in their dealings with suppliers and customers; a rule that requires any employee who receives from a supplier or customer a gift worth more than \$10 to report the gift; and an SOP that obliges the recipient of the gift to make the disclosure in writing within 30 days.

In contrast, *single-use plans* are developed to handle nonprogrammed decision making in unusual or one-of-a-kind situations. Examples of single-use plans include *programs*, which are integrated sets of plans for achieving certain goals, and *projects*, which are specific action plans created to complete various aspects of a program. One of NASA's major programs was to reach the moon, and one project in this program was to develop a lunar module capable of landing on the moon and returning to the earth.

Why planning is important

Essentially, planning is ascertaining where an organization is at the present time and deciding where it should be in the future and how to move it forward. When managers plan, they must consider the future and forecast what may happen in order to take actions in the present and mobilize organizational resources to deal with future opportunities and threats. As we have discussed in previous chapters, however, the external environment is uncertain and complex, and managers typically must deal with incomplete information and bounded rationality. This is one reason why planning is so complex and difficult.

Almost all managers engage in planning, and all should participate because they must try to predict future opportunities and threats. The absence of a plan often results in hesitations, false steps, and mistaken changes of direction that can hurt an organization or even lead to disaster. Planning is important for four main reasons:

1. Planning is a useful way of getting managers to participate in decision making about the appropriate goals and strategies for an organization. Effective planning gives all managers the opportunity to participate in decision making. At Intel, for example, top managers, as part of their annual planning process, regularly request input from lower-level managers to determine what the organization's goals and strategies should be.
2. Planning is necessary to give the organization a sense of direction and purpose.⁹ A plan states what goals an organization is trying to achieve and what strategies it intends to use to achieve them. Without the sense of direction and purpose that a formal plan provides, managers may interpret their own tasks and roles in ways that best suit themselves. The result will be an organization that is pursuing

multiple and often conflicting goals and a set of managers who do not cooperate and work well together. By stating which organizational goals and strategies are important, a plan keeps managers on track so that they use the resources under their control effectively.

3. A plan helps coordinate managers of the different functions and divisions of an organization to ensure that they all pull in the same direction. Without a good plan, it is possible that the members of the manufacturing function will produce more products than the members of the sales function can sell, resulting in a mass of unsold inventory. Implausible as this might seem, it happened to the high-flying Internet router supplier Cisco Systems in the early 2000s when manufacturing, which had been able to sell all the routers that it produced, found it had over \$2 billion of unsold inventory because of the combination of an economic recession and customers' demands for new kinds of optical routers that Cisco did not have in stock.

4. A plan can be used as a device for controlling managers within an organization. A good plan specifies not only which goals and strategies the organization is committed to but also who is responsible for putting the strategies into action to attain the goals. When managers know that they will be held accountable for attaining a goal, they are motivated to do their best to make sure the goal is achieved.

Henri Fayol, the originator of the model of management we discussed in Chapter 1, said that effective plans should have four qualities: unity, continuity, accuracy, and flexibility.¹⁰ *Unity* means that at any one time only one central, guiding plan is put into operation to achieve an organizational goal; more than one plan to achieve a goal would cause confusion and disorder. *Continuity* means that planning is an ongoing process in which managers build and refine previous plans and continually modify plans at all levels—corporate, business, and functional—so that they fit together into one broad framework. *Accuracy* means that managers need to make every attempt to collect and utilize all available information at their disposal in the planning process. Of course, managers must recognize the fact that uncertainty exists and that information is almost always incomplete (for reasons we discussed in Chapter 6). Despite the need for continuity and accuracy, however, Fayol emphasized that the planning process should be *flexible* enough so that plans can be altered and changed if the situation changes; managers must not be bound to a static plan.

Scenario planning

One way in which managers can try to create plans that have the four qualities that Fayol described is by utilizing scenario planning, one of the most widely used planning techniques. **Scenario planning** (also known as *contingency planning*) is the generation of multiple forecasts of future conditions followed by an analysis of how to respond effectively to each of those conditions.

As noted previously, planning is about trying to forecast and predict the future in order to be able to anticipate future opportunities and threats. The future, however, is inherently unpredictable. How can managers best deal with this unpredictability? This question preoccupied managers at Royal Dutch Shell, the third-largest global oil company in the 1980s. In 1984, oil was \$30 a barrel, and most analysts and managers, including Shell's, believed that it would hit \$50 per

scenario planning

The generation of multiple forecasts of future conditions followed by an analysis of how to respond effectively to each of those conditions; also called *contingency planning*.

barrel by 1990. Nevertheless, Shell conducted a scenario-planning exercise for its managers. Shell's managers were asked to use scenario planning to generate different future scenarios of conditions in the oil market and then to develop a set of plans that detailed how they would respond to these opportunities and threats if any such scenario occurred.

One scenario used the assumption that oil prices would fall to \$15 per barrel, and managers had to decide what they should do in such a case. Managers went to work with the goal of creating a plan consisting of a series of recommendations. The final plan included proposals to cut oil exploration costs by investing in new technologies, to accelerate investments in cost-efficient oil-refining facilities, and to weed out unprofitable gas stations.¹¹ In reviewing these proposals, top management came to the conclusion that even if oil prices continued to rise, all of these actions would benefit Shell by widening the company's profit margin. They decided to put the plan into action. As it happened, in the mid-1980s oil prices did collapse to \$15 a barrel, but Shell, unlike its competitors, had already taken steps to be profitable in a low-oil-price world. Consequently, by 1990, the company was twice as profitable as its major competitors.

Because the future is unpredictable, the only reasonable approach to planning is first to generate "multiple futures"—or scenarios of the future—based on different assumptions about conditions that *might prevail* in the future and then to develop different plans that detail what a company *should do* in the event that one of these scenarios actually occurs. Scenario planning is a learning tool that raises the quality of the planning process and can bring real benefits to an organization.¹² Shell's success with scenario planning influenced many other companies to adopt similar systems. By 1990, more than 50 percent of Fortune 500 companies were using some version of scenario planning, and the number has increased since then.¹³ The great strength of scenario planning is its ability not only to anticipate the challenges of an uncertain future but also to educate managers to think about the future—to *think strategically*.¹⁴

Determining the Organization's Mission and

Goals Defining the business

Determining the organization's mission and goals is the first step of the planning process. Once the mission and goals are agreed upon and formally stated in the corporate plan, they guide the next steps by defining which strategies are appropriate and which are inappropriate.¹⁵

To determine an organization's mission, managers must first define its business so that they can identify what kind of value they will provide to customers. To define the business, managers must ask three questions: (1) Who are our customers? (2) What customer needs are being satisfied? (3) How are we satisfying customer needs?¹⁶ They ask these questions to identify the customer needs that the organization satisfies and the way the organization satisfies those needs. Answering these questions helps managers to identify not only the customer needs they are satisfying now but the needs they should try to satisfy in the future and who their true competitors are. All of this information helps managers plan and establish appropriate goals. The case of Mattel shows the important role that defining the business has in the planning process.



Ups and Downs at Mattel

In the 1990s, Mattel Inc., the well-known maker of such classic toys as Barbie dolls and Hot Wheels, believed that the toy market and customer preferences for toys were changing rapidly. This was because of the growing popularity of electronic toys and computer games. Sales of computer games had increased dramatically as more and more parents saw the educational opportunities offered by games that children would enjoy playing. Moreover, many kinds of computer games could be played with other people over the Internet, so it seemed that in the future the magic of electronics and information technology would turn the toy world upside down. Mattel's managers feared that core products, such as its range of Barbie dolls, might lose their appeal and become passé given the future possibilities opened up by chips, computers, and the Internet. Mattel's managers believed that its customers' needs were changing and that the company needed to find new ways to satisfy those needs if it was to remain the biggest toy seller in the United States. Fearing they would lose their customers to the new computer game companies, Mattel's managers decided that the quickest and easiest way to redefine its business and become a major player in the computer game market would be to acquire one of these companies. So in 1998 Mattel paid \$3.5 billion for The Learning Company, the maker of such popular games as "Thinking Things." Its goal was to use this company's expertise and knowledge both to build an array of new computer games and to take Mattel toys such as Barbie and create new games around them. In this way Mattel hoped to better meet the needs of its existing customers and cater to the needs of the new computer game customers.¹⁷

In addition, while some classic toys like Barbie have the potential to satisfy customers' needs for generations, the popularity of many toys is temporary and is often linked to the introduction of a new movie from Disney, Pixar, or Dreamworks. To ensure that it could meet the changing needs of customers for these kinds of toys, Mattel contracted with the three film companies to become the supplier of the toys linked to their movies. For example, in 2001 it agreed to pay Warner Brothers 15 percent of the gross revenues, and a guaranteed \$20 million, for the rights to produce toys linked to the Harry Potter movie, based on the books of the same name. It launched a line of toys, filled with electronics, that allow them to move and make sounds and also created Harry Potter computer games that satisfied its customers' needs.¹⁸

While Mattel's managers correctly sensed that customers' needs were changing, the way in which it decided to satisfy customers new needs—namely, by buying The Learning Company—was not the right decision. It turned out that the skills required to rapidly develop new games linked to Mattel's products were not present in The Learning Company and few popular games were forthcoming. Moreover, Mattel had underestimated the need to promote and update its core toys, and the \$3.5 billion could have been much better spent boosting and developing these toys. In 2001, CEO Bob Eckert sold The Learning Company and decided that henceforth Mattel would hire independent specialist companies to develop new electronic toys and computer games, including many related to its well-known products.

In the fast-paced toy market where customers' needs change and evolve, and where new groups of customers emerge as new technologies result in new kinds



One of the new Harry Potter products: a life-sized replica of "Fluffy" the three-headed dog that guards the Sorcerer's Stone in the popular book series. Mattel has a license to manufacture and sell a whole range of Harry Potter products.

girls. As Mattel's experience suggests, companies have to listen closely to their customers and decide how best to meet their changing needs and preferences.

of toys, toy companies like Mattel must learn to define and redefine their businesses to satisfy those needs. By 2001, Mattel had begun to turn out whole new ranges of electronic products linked to Barbie, a new Diva Starz doll line, and new electronic games, and its profits started to recover in the early 2000s.

In 2004, however, sales of Barbie products faltered; international Barbie sales dipped by 11 percent and domestic sales by 15 percent. In July 2004 Eckert announced, "Our biggest challenge ahead is reinvigorating the fashion (doll) business. We're directing tremendous time, energy and resources to regain our momentum in the fashion doll category."¹⁹ Mattel is continuing to revamp the Barbie product line, incorporating themes and story lines into the brand in hopes it will widen the dolls' appeal, particularly with 8- to 10-year-old

Establishing major goals

Once the business is defined, managers must establish a set of primary goals to which the organization is committed. Developing these goals gives the organization a sense of direction or purpose. In most organizations, articulating major goals is the job of the CEO, although other managers have input into the process. Thus, at Mattel, CEO Eckert operates with the primary goal of being the leader in every segment of the toy market in which the company competes.

The best statements of organizational goals are ambitious—that is, they stretch the organization and require that managers improve its performance capabilities.²⁰ For example, in 2001 Cisco Systems CEO John Chambers outlined a very challenging goal. This Internet hardware company had been the success story of the 1990s. Cisco had enjoyed yearly growth of 30 to 50 percent in sales revenue, but it was hit in 2000 with over \$2.2 billion in excess inventory it could not sell as many of the dot-com companies went belly up and its sales plummeted.²¹ Nevertheless, Chambers announced that the company intended to return to its 30 to 50 percent growth rate within three years and was taking the appropriate steps to get there—steps that included the firing of thousands of employees, a big push to increase global sales, and the investment of billions in research to produce new

Figure 6.4
Three Mission Statements

COMPANY	MISSION STATEMENT
Cisco	Cisco solutions provide competitive advantage to our customers through more efficient and timely exchange of information, which in turn leads to cost savings, process efficiencies, and closer relationships with our customers, prospects, business partners, suppliers, and employees.
Wal-Mart	We work for you. We think of ourselves as buyers for our customers, and we apply our considerable strengths to get the best value for you. We've built Wal-Mart by acting on behalf of our customers, and that concept continues to propel us. We're working hard to make our customers' shopping easy.
AT&T	We are dedicated to being the world's best at bringing people together—giving them easy access to each other and to the information and services they want and need—anytime, anywhere.

generations of optical networking equipment. This goal represented a significant challenge for Cisco because by the top-management team's own admission, many of its largest customers were cutting back on Internet expenditures and the dot-com boom was over. In fact, Cisco did not achieve its ambitious growth rate because of the recession of the early 2000s; however, its financial performance did improve dramatically, and Cisco maintained its competitive advantage over its industry rivals because of its new strategies. Cisco's managers' vision of the mission and goals of their company, along with the managerial visions at AT&T and Wal-Mart, is presented in Figure 6.4.

Although goals should be challenging, they should also be realistic. Challenging goals give managers an incentive to look for ways to improve an organization's operation, but a goal that is unrealistic and impossible to attain may prompt managers to give up.²² For example, Cisco set the challenging, realistic goal of reducing its costs by \$1 billion a year, and managers were able to improve the efficiency of Cisco's operations and achieve this goal.²³

The time period in which a goal is expected to be achieved should be stated. Cisco's managers committed themselves to achieving the sales increases by 2004, but conditions in the global environment prevented this and now their goal is 2006. Time constraints are important because they emphasize that a goal must be attained within a reasonable period; they inject a sense of urgency into goal attainment and act as a motivator.

strategy formulation

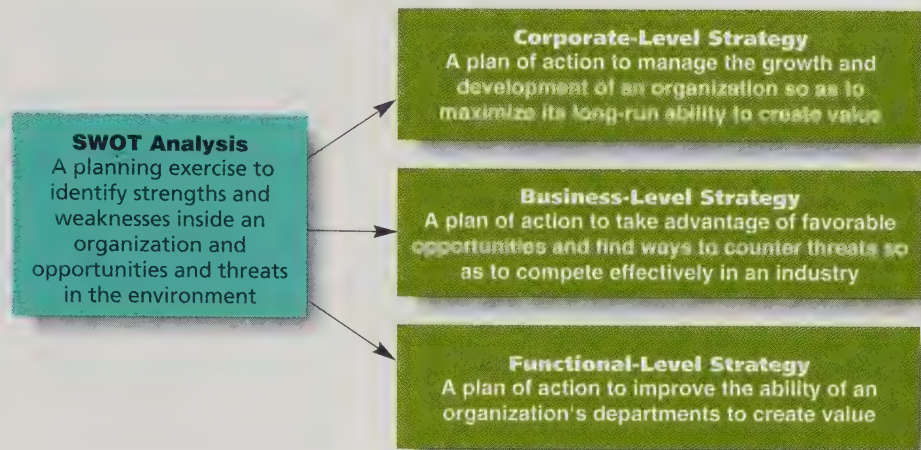
Analysis of an organization's current situation followed by the development of strategies to accomplish its mission and achieve its goals.

Formulating Strategy

In **strategy formulation** managers analyze an organization's current situation and then develop strategies to accomplish an organization's mission and achieve its goals.²⁴

Strategy formulation begins with managers analyzing the factors within an organization and outside in the global environment that affect or may affect the organization's ability to meet its goals now and in the future. SWOT analysis and the five forces model are two useful techniques managers use to analyze these factors.

Figure 6.5
Planning and
Strategy
Formulation



SWOT analysis

SWOT analysis A planning exercise in which managers identify organizational strengths (S), weaknesses (W), environmental opportunities (O), and threats (T).

SWOT analysis is a planning exercise in which managers identify organizational strengths (S), weaknesses (W), environmental opportunities (O), and threats (T). Based on a SWOT analysis, managers at the different levels of the organization select the corporate-, business-, and functional-level strategies to best position the organization to achieve its mission and goals (see Figure 6.5). Because SWOT analysis is the first step in strategy formulation at any level, we consider it first, before turning specifically to corporate-, business-, and functional-level strategies.

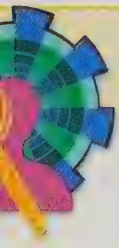
In Chapter 6 we discussed forces in the task and general environments that have the potential to affect an organization. We noted that changes in these forces can produce opportunities that an organization might take advantage of and threats that may harm its current situation. The first step in SWOT analysis is to identify an organization's strengths and weaknesses. Table 6.1 (page 214) lists many important strengths (such as high-quality skills in marketing and in research and development) and weaknesses (such as rising manufacturing costs and outdated technology). The task facing managers is to identify the strengths and weaknesses that characterize the present state of their organization.

The second step in SWOT analysis begins when managers embark on a full-scale SWOT planning exercise to identify potential opportunities and threats in the environment that affect the organization at the present or may affect it in the future. Examples of possible opportunities and threats that must be anticipated are listed in Table 6.1.

With the SWOT analysis completed, and strengths, weaknesses, opportunities, and threats identified, managers can begin the planning process and determine strategies for achieving the organization's mission and goals. The resulting strategies should enable the organization to attain its goals by taking advantage of opportunities, countering threats, building strengths, and correcting organizational weaknesses. To appreciate how managers use SWOT analysis to formulate strategy, consider how Douglas Conant, CEO of Campbell Soup, has used it to try to find strategies to turn around the troubled food products maker.

Table 6.1
Questions for SWOT Analysis

Potential Strengths	Potential Opportunities	Potential Weaknesses	Potential Threats
Well-developed strategy?	Expand core business(es)?	Poorly developed strategy?	Attacks on core business(es)?
Strong product lines?	Exploit new market segments?	Obsolete, narrow product lines?	Increase in domestic competition?
Broad market coverage?	Widen product range?	Rising manufacturing costs?	Increase in foreign competition?
Manufacturing competence?	Extend cost or differentiation advantage?	Decline in R&D innovations?	Change in consumer tastes?
Good marketing skills?	Diversify into new growth businesses?	Poor marketing plan?	Fall in barriers to entry?
Good materials management systems?	Expand into foreign markets?	Poor materials management systems?	Rise in new or substitute products?
R&D skills and leadership?	Apply R&D skills in new areas?	Loss of customer goodwill?	Increase in industry rivalry?
Human resource competencies?	Enter new related businesses?	Inadequate human resources?	New forms of industry competition?
Brand-name reputation?	Vertically integrate forward?	Loss of brand name?	Potential for takeover?
Cost of differentiation advantage?	Vertically integrate backward?	Growth without direction?	Changes in demographic factors?
Appropriate management style?	Overcome barriers to entry?	Loss of corporate direction?	Changes in economic factors?
Appropriate organizational structure?	Reduce rivalry among competitors?	Infighting among divisions?	Downturn in economy?
Appropriate control systems?	Apply brand-name capital in new areas?	Loss of corporate control?	Rising labor costs?
Ability to manage strategic change?	Seek fast market growth?	Inappropriate organizational structure and control systems?	Slower market growth?
Others?	Others?	High conflict and politics?	Others?
		Others?	



Manager as a Person

Douglas Conant Is in the Soup

Campbell Soup Co. is one of the oldest and best-known companies in the world. However, in recent years Campbell has seen demand for its major products like condensed soup plummet as customers have switched from high-salt, processed soups to healthier low-fat, low-salt varieties. Indeed, its condensed soup business fell by 30 percent between 1998 and 2004. By the early 2000s Campbell's market share and profits were falling, and its new CEO Douglas



As part of an attempt to turn around its ailing condensed soup business, Campbell's used some innovative marketing plays. Here Steve Solomon puts the finishing touches on a 10-foot-tall Campbell's Tomato Soup can displaying the company's newly designed soup label. It was unveiled at the Andy Warhol Museum in Pittsburgh, the home of many of Warhol's pop art Campbell's Soup pictures.

Conant decided it was necessary to devise a three-year turnaround plan to help the company maintain its market position.

One of Conant's first actions was to initiate a thorough SWOT planning exercise. An analysis of the environment identified the growth of the organic- and health-food segment of the food market and the increasing number of other kinds of convenience foods as a threat to Campbell's core soup business. The analysis of the environment also revealed three growth opportunities: (1) the growing market for health and sports drinks, in which Campbell already was a competitor with its V8 juice, (2) the growing market for salsas, in which Campbell competed with its Pace salsa, and (3) chocolate products, where Campbell's Godiva brand had enjoyed increasing sales throughout the 1990s.

With the analysis of the environment complete, Conant turned his attention to his organization's resources and capabilities. His internal analysis of Campbell identified a number of major weaknesses. These included staffing levels that were too high relative to its competitors and high costs associated with manufacturing its soups because of the use of outdated machinery. Also, Conant noted that Campbell had a very conservative culture in which

people seemed to be afraid to take risks—something that was a real problem in the fast-changing food industry, where customer tastes are always changing and new products must be developed constantly. At the same time, the SWOT analysis identified an enormous strength: Campbell enjoyed huge economies of scale because of the enormous quantity of food products that it makes, and it also had a first-rate research and development division that had the capability to develop exciting new food products.

Using the information gained from this SWOT analysis, Conant and his managers decided that Campbell needed to use its product development skills to revitalize its core products and modify or reinvent them in ways that would appeal to increasingly health-conscious and busy consumers who did not want to take the time to prepare old-fashioned condensed soup. Moreover, it needed to expand its franchise in the health- and sports-, snack-, and luxury-food segments of the market. Another major need that managers saw was to find new ways to deliver Campbell's products to customers. To increase sales, Campbell's needed to tap into new food outlets, such as corporate cafeterias, college dining halls, and other mass eateries, to expand consumers' access to its foods. Finally, Conant decided it was necessary to decentralize authority to managers at lower levels in the organization and give them the responsibility of bringing new kinds of soups, salsas, and chocolate products to the market. In this way he hoped to revitalize Campbell's slow-moving culture and speed the flow of improved and new products to the market.

Conant put his new plan into action, sales of soup started to rise, and he began to put more emphasis on sales of soup at outlets such as 7-11 and Subway and less on supermarket sales.²⁵ By 2004, analysts felt that Conant had made a significant difference in Campbell's performance but that there was still a lot to do as Campbell's operating margins were still shrinking. Carrying on the SWOT analysis, Conant decided Campbell should produce more products to meet the needs of the "low-carb diet," such as new kinds of low-carb bread and cookies. He also decided to shrink the company's operations to lower costs. His goal is to raise profit margins to the level of his major competitors Kraft and General Mills by 2007 using a new three-year plan based on this SWOT analysis.²⁶

The five forces model

A well-known model that helps managers isolate particular forces in the external environment that are potential threats is Michael Porter's five forces model. Porter identified these five factors that are major threats because they affect how much profit organizations competing within the same industry can expect to make:

- *The level of rivalry among organizations in an industry.* The more that companies compete against one another for customers—for example, by lowering the prices of their products or by increasing advertising—the lower is the level of industry profits (low prices mean less profit).
- *The potential for entry into an industry.* The easier it is for companies to enter an industry—because, for example, barriers to entry, such as brand loyalty, are low—the more likely it is for industry prices and therefore industry profits to be low.
- *The power of suppliers.* If there are only a few suppliers of an important input, then suppliers can drive up the price of that input, and expensive inputs result in lower profits for the producer.
- *The power of customers.* If only a few large customers are available to buy an industry's output, they can bargain to drive down the price of that output. As a result, producers make lower profits.
- *The threat of substitute products.* Often, the output of one industry is a substitute for the output of another industry (plastic may be a substitute for steel in some applications, for example; similarly, bottled water is a substitute for cola). Companies that produce a product with a known substitute cannot demand high prices for their products, and this constraint keeps their profits low.

Porter argued that when managers analyze opportunities and threats they should pay particular attention to these five forces because they are the major threats that an organization will encounter. It is the job of managers at the corporate, business, and functional levels to formulate strategies to counter these threats so that an organization can respond to its task and general environments, perform at a high level, and generate high profits. At Campbell Conant performs such an analysis to identify the opportunities and threats stemming from the actions of food industry rivals.

Formulating Corporate-Level Strategies

Corporate-level strategy is a plan of action concerning which industries and countries an organization should invest its resources in to achieve its mission and goals. In developing a corporate-level strategy, managers ask: How should the growth and development of the company be managed in order to increase its ability to create value for its customers (and thus increase performance) over the long run? Managers of most organizations have the goal of growing their companies and actively seek out new opportunities to use the organization's resources to create more goods and services for customers. Examples of organizations growing rapidly are Google, chip maker AMD, Hyundai, and Toyota, whose managers pursue any feasible opportunity to use their companies' skills to provide customers with new products.

In addition, some managers must help their organizations respond to threats due to changing forces in the task or general environment. For example, customers may no longer be buying the kinds of goods and services a company is producing (bulky computer monitors or televisions), or other organizations may have entered the market and attracted away customers (this happened to Intel when AMD began to produce more powerful chips). Top managers aim to find the best strategies to help the organization respond to these changes and improve performance.

The principal corporate-level strategies that managers use to help a company grow, to keep it on top of its industry, and to help it retrench and reorganize to stop its decline are (1) concentration on a single business, (2) diversification, (3) international expansion, and (4) vertical integration. These four strategies are all based on one idea: An organization benefits from pursuing any one of them only when the strategy helps further increase the value of the organization's goods and services for customers. To increase the value of goods and services, a corporate-level strategy must help an organization, or one of its divisions, differentiate and add value to its products either by making them unique or special or by lowering the costs of value creation.

Concentration on a single business

Most organizations begin their growth and development with a corporate-level strategy aimed at concentrating resources in one business or industry in order to develop a strong competitive position within that industry. For example, McDonald's began as one restaurant in California, but its managers' long-term goal was to focus its resources in the fast-food business and use those resources to quickly expand across the United States.

Sometimes, concentration on a single business becomes an appropriate corporate-level strategy when managers see the need to reduce the size of their organizations to increase performance. Managers may decide to get out of certain industries, for example, when particular divisions lose their competitive advantage. Managers may sell off those divisions, lay off workers, and concentrate remaining organizational resources in another market or business to try to improve performance. This happened to electronics maker Hitachi when it was forced to get out of the CRT computer monitor business. Intense low-price competition existed in the computer monitor market because customers were increasingly switching from bulky CRT monitors to the newer, flat, LCD monitors. Hitachi announced it was closing three

factories in Japan, Singapore, and Malaysia that produced CRT monitors and would use its resources to invest in the new LCD technology.²⁷ In contrast, when organizations are performing effectively, they often decide to enter new industries in which they can use their resources to create more value.

Diversification

diversification

Expanding operations into a new business or industry and producing new goods or services.

related diversification

Entering a new business or industry to create a competitive advantage in one or more of an organization's existing divisions or businesses.

synergy Performance gains that result when individuals and departments coordinate their actions.

unrelated diversification

Entering a new industry or buying a company in a new industry that is not related in any way to an organization's current businesses or industries.

Diversification is the strategy of expanding operations into a new business or industry and producing new goods or services.²⁸ Examples of diversification include PepsiCo's diversification into the snack-food business with the purchase of Frito Lay, tobacco giant Philip Morris's diversification into the brewing industry with the acquisition of Miller Beer, and General Electric's move into broadcasting with its acquisition of NBC. There are two main kinds of diversification: related and unrelated.

RELATED DIVERSIFICATION **Related diversification** is the strategy of entering a new business or industry to create a competitive advantage in one or more of an organization's existing divisions or businesses. Related diversification can add value to an organization's products if managers can find ways for its various divisions or business units to share their valuable skills or resources so that synergy is created.²⁹ **Synergy** is obtained when the value created by two divisions cooperating is greater than the value that would be created if the two divisions operated separately. For example, suppose two or more divisions within a diversified company can utilize the same manufacturing facilities, distribution channels, advertising campaigns, and so on. Each division that shares resources has to invest less in the shared functions than it would have to invest if it had full responsibility for the activity. In this way, related diversification can be a major source of cost savings.³⁰ Similarly, if one division's R&D skills can be used to improve another division's products, the second division's products may receive a competitive advantage.

Procter & Gamble's disposable diaper and paper towel businesses offer one of the best examples of the successful production of synergies. These businesses share the costs of procuring inputs such as paper and developing new technology to reduce manufacturing costs. In addition, a joint sales force sells both products to supermarkets, and both products are shipped by means of the same distribution system. This resource sharing has enabled both divisions to reduce their costs, and as a result, they can charge lower prices than their competitors and thus attract more customers.³¹

In pursuing related diversification, managers often seek to find new businesses where they can use the existing skills and resources in their departments to create synergies, add value to the new business, and hence improve the competitive position of the company. Alternatively, managers may acquire a company in a new industry because they believe that some of the skills and resources of the acquired company might improve the efficiency of one or more of their existing divisions. If successful, such skill transfers can help an organization to lower its costs or better differentiate its products because they create synergies between divisions.

UNRELATED DIVERSIFICATION Managers pursue **unrelated diversification** when they enter new industries or buy companies in new industries that

are not related in any way to their current businesses or industries. One main reason for pursuing unrelated diversification is that, sometimes, managers can buy a poorly performing company, transfer their management skills to that company, turn around its business, and increase its performance, all of which creates value.

Another reason for pursuing unrelated diversification is that purchasing businesses in different industries lets managers engage in *portfolio strategy*, which is apportioning financial resources among divisions to increase financial returns or spread risks among different businesses, much as individual investors do with their own portfolios. For example, managers may transfer funds from a rich division (a “cash cow”) to a new and promising division (a “star”) and, by appropriately allocating money between divisions, create value. Though used as a popular explanation in the 1980s for unrelated diversification, portfolio strategy ran into increasing criticism in the 1990s.³²

Indeed, more and more companies and their managers have abandoned the strategy of unrelated diversification because there is evidence that too much diversification can cause managers to lose control of their organization’s core business. Management experts suggest that although unrelated diversification might initially create value for a company, managers sometimes use portfolio strategy to expand the scope of their organization’s businesses too much. When this happens, it becomes difficult for top managers to be knowledgeable about all of the organization’s diverse businesses. Managers do not have the time to process all of the information required to adequately assess the strategy and performance of each division objectively, and organizational performance often suffers.

This problem began to occur at General Electric in the 1970s. As former CEO Reg Jones commented: “I tried to review each business unit plan in great detail. This effort took untold hours and placed a tremendous burden on the corporate executive office. After awhile I began to realize that no matter how hard we would work, we could not achieve the necessary in-depth understanding of the 40-odd business unit plans.”³³ Unable to handle so much information, top managers are overwhelmed and eventually make important resource allocation decisions on the basis of only a superficial analysis of the competitive position of each division. This usually results in value being lost rather than created.³⁴

Thus, although unrelated diversification can create value for a company, research evidence suggests that many diversification efforts have reduced value rather than created it.³⁵ As a consequence, during the 1990s there was a trend among many diversified companies to divest many of their unrelated divisions. Managers sold off divisions and concentrated organizational resources on their core business, focusing more on related diversification.³⁶ In the 1990s, for example, Sears divested all of the stock brokerage, insurance, and real-estate businesses it had acquired during the 1980s and concentrated on strengthening its core retailing activities to survive in its fight with Wal-Mart and Target.

International expansion

As if planning the appropriate level of diversification were not a difficult enough decision, corporate-level managers also must decide on the appropriate way to compete internationally. A basic question confronts the managers of any organization that competes in more than one national market: To what extent should the

organization customize features of its products and marketing campaign to different national conditions?³⁷

If managers decide that their organization should sell the same standardized product in each national market in which it competes, and use the same basic marketing approach, they adopt a **global strategy**.³⁸ Such companies undertake very little, if any, customization to suit the specific needs of customers in different countries. But if managers decide to customize products and marketing strategies to specific national conditions, they adopt a **multidomestic strategy**. Matsushita, with its Panasonic brand, has traditionally pursued a global strategy, selling the same basic TVs and VCRs in every market in which it does business and often using the same basic marketing approach. Unilever, the European food and household products company, has pursued a multidomestic strategy. Thus, to appeal to German customers, Unilever's German division sells a different range of food products and uses a different marketing approach than its North American division.

Global and multidomestic strategies both have advantages and disadvantages. The major advantage of a global strategy is the significant cost savings associated

with not having to customize products and marketing approaches to different national conditions. For example, Rolex watches, Ralph Lauren or Tommy Hilfiger clothing, Channel or Armani accessories or perfume, Dell computers, Chinese-made plastic toys and buckets, and U.S.-grown rice and wheat are all products that can be sold using the same marketing across many countries by simply changing the language. Thus, companies can save a significant amount of money. The major disadvantage of pursuing a global strategy is that, by ignoring national differences, managers may leave themselves vulnerable to local competitors that do differentiate their products to suit local tastes. This occurred in the British consumer electronics industry. Amstrad, a British computer and electronics company, got its start by recognizing and responding to local consumer needs. Amstrad captured a major share of the British audio market by ignoring the standardized inexpensive music centers marketed by companies pursuing a global strategy, such as Sony and Matsushita. Instead, Amstrad's product was encased in teak rather than metal and featured a control panel tailor-made to appeal to British consumers' preferences. To remain competitive in this market, Matsushita had to place more emphasis on local customization of its Panasonic and JVC brands.

The advantages and disadvantages of a multidomestic strategy are the opposite of those of a global strategy. The major advantage of a multidomestic strategy is that by customizing product offerings and marketing approaches to local

global strategy

Selling the same standardized product and using the same basic marketing approach in each national market.

multidomestic strategy

Customizing products and marketing strategies to specific national conditions.



A study in contrasts. Matsushita, with its Panasonic brand (shown on the top), has pursued largely a global strategy, selling the same basic TVs and VCRs in every market and using a similar marketing message. Unilever, on the other hand, has pursued a multidomestic strategy, tailoring its product line and marketing approach to specific locations. On the bottom, the CEO of Hindustan Lever, Ltd., Keki Dadiseth, holds a box of Surf detergent.

conditions, managers may be able to gain market share or charge higher prices for their products. The major disadvantage is that customization raises production costs and puts the multidomestic company at a price disadvantage because it often has to charge prices higher than the prices charged by competitors pursuing a global strategy. Obviously, the choice between these two strategies calls for trade-offs.

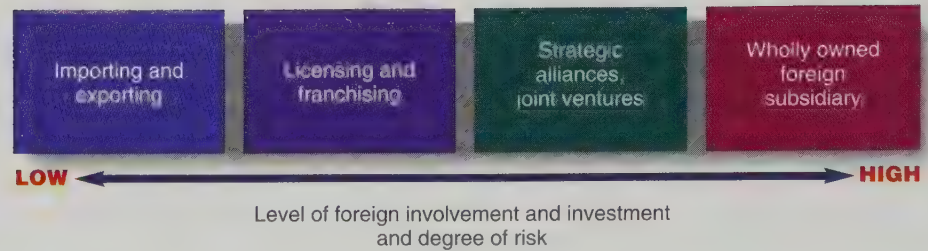
Managers at Gillette, the well-known razor blade maker, created a strategy that combines the best features of both international strategies. Gillette has been a global company from the beginning, as its managers quickly saw the advantages of selling its razor blades abroad. By 2004, 65 percent of Gillette's revenues came from global sales, and this percentage is expected to increase.³⁹ Gillette's strategy over the years has been pretty constant: Find a new foreign country with a growing market for razor blades, form a strategic alliance with a local razor blade company and take a majority stake in it, invest in a large marketing campaign, and then build a modern factory to make razor blades and other products for the local market. For example, when Gillette entered Russia after the breakup of the Soviet Union, it saw a huge opportunity to increase sales. It formed a joint venture with a local company called Lenincts Concern, which made a razor known as the Sputnik, and then with this base began to import its own brands into Russia. When sales growth rose sharply, Gillette decided to offer more products in the market and built a new plant in St. Petersburg.⁴⁰

In 2005, Gillette operated 50 manufacturing facilities in more than 20 countries.⁴¹ It established its factories in countries where labor and other costs were low and then distributed and marketed its products to countries in that region of the world. In this sense it pursues a global strategy. However, all of Gillette's research and development and design take place in the United States. As it develops new kinds of razors, it equips its foreign factories to manufacture them when it decides that local customers are ready to trade up to the new product. So, for example, Gillette's latest razor may be introduced in a foreign country years later than in the United States. Thus, Gillette is customizing its product offering to the needs of different countries and also pursues a multidomestic strategy. By pursuing this international strategy, Gillette achieves low costs and still differentiates and customizes its product range to suit the needs of each country or world region. This strategy has proved very effective for Gillette, whose global sales and profits continue to increase, so much so that in 2005 Procter & Gamble announced its intention to buy Gillette and merge its operations into its own.

CHOOSING A WAY TO EXPAND INTERNATIONALLY As we have discussed, a more competitive global environment has proved to be both an opportunity and a threat for organizations and managers. The opportunity is that organizations that expand globally are able to open new markets, reach more customers, and gain access to new sources of raw materials and to low-cost suppliers of inputs. The threat is that organizations that expand globally are likely to encounter new competitors in the foreign countries they enter and must respond to new political, economic, and cultural conditions.

Before setting up foreign operations, managers of companies such as Amazon.com, Lands' End, GE, Toys 'R' Us, and Boeing needed to analyze the forces in the environment of a particular country (such as Korea or Brazil) in order to choose the right method to expand and respond to those forces in the most appropriate way. In general, four basic ways to operate in the global environment are

Figure 6.6
Four Ways of
Expanding
Internationally



importing and exporting, licensing and franchising, strategic alliances, and wholly owned foreign subsidiaries, Gillette's preferred approach. We briefly discuss each one, moving from the lowest level of foreign involvement and investment required of a global organization and its managers, and the least amount of risk, to the high end of the spectrum (see Figure 6.6).⁴²

exporting Making products at home and selling them abroad.

importing Selling at home products that are made abroad.

IMPORTING AND EXPORTING The least complex global operations are exporting and importing. A company engaged in **exporting** makes products at home and sells them abroad. An organization might sell its own products abroad or allow a local organization in the foreign country to distribute its products. Few risks are associated with exporting because a company does not have to invest in developing manufacturing facilities abroad. It can further reduce its investment abroad if it allows a local company to distribute its products.

A company engaged in **importing** sells at home products that are made abroad (products it makes itself or buys from other companies). For example, most of the products that Pier 1 Imports, The Bombay Company, and The Limited sell to their customers are made abroad. In many cases the appeal of a product—Irish glass, French wine, Italian furniture, or Indian silk—is that it is made abroad. The Internet has made it much easier for companies to inform potential foreign buyers about their products; detailed product specifications and features are available online, and informed buyers can communicate easily with prospective sellers. The way in which Levi Strauss was forced to change its international approach from exporting to importing illustrates how the growth of low-cost manufacturing abroad has changed competition in many industries.



Managing Globally

Levi Strauss's Big Problems

Levi Strauss, the well-known jeans maker, was once the global leader in the apparel industry. Its jeans commanded a premium price as customers the world over perceived the value or status of wearing Levi jeans was worth paying extra for. Indeed, in Europe and Asia, Levi jeans were often sold at double or triple their U.S. price. No more. Levi is now fighting to lower its costs to be able to survive in the fast-changing jeans industry.

Levi's problems arose because of changes in the international strategies of other jeans makers and apparel companies. Early in the 1990s, other jeans makers such as VF Corp (which makes Wrangler jeans), Calvin Klein, and Polo outsourced the production of jeans to countries abroad where labor costs were lowest. With their lower costs, these companies then began to charge lower



Jean manufacturers have lowered costs by outsourcing production to countries abroad.

prices for their products and customers began to switch to buying their jeans. Then, in a significant move, apparel companies such as Wal-Mart, JCPenney, Sears, and Dillard's began to wonder why they should pay Levi a premium price for selling its jeans when they could sell jeans under their own labels at a lower price and still make more profit than if they sold Levi's jeans. So they contracted with low-cost foreign producers to make jeans under their own in-house labels. The result was that sales of Levi jeans plummeted as many customers began to buy jeans on the basis of their price.

Levi, because it still produced most of its jeans in the United States and exported them abroad, was caught unprepared and found it could no longer compete. It lost billions of dollars in the 1990s as sales plummeted; to survive, it was forced to change from exporting its jeans to importing its jeans from abroad—it outsourced all production to manufacturers abroad. Since 1997 it has closed all 35 of its U.S. manufacturing facilities and laid off over 30,000 employees.

Once it outsourced production abroad, Levi was able to reduce its prices to be competitive. Indeed, its prices fell so low that Wal-Mart began to sell Levi jeans in its stores. However, low prices mean low profits, and Levi's problems have continued into the 2000s as it struggles to find a way to compete successfully in a global market dominated by ruthless low-cost/price competition.

licensing Allowing a foreign organization to take charge of manufacturing and distributing a product in its country or world region in return for a negotiated fee.

LICENSING AND FRANCHISING In **licensing**, a company (the licensor) allows a foreign organization (the licensee) to take charge of both manufacturing and distributing one or more of its products in the licensee's country or world region in return for a negotiated fee. Chemical maker Du Pont might license a local factory in India to produce nylon or Teflon. The advantage of licensing is that the licensor does not have to bear the development costs associated with opening up in a foreign country; the licensee bears the costs. The risks associated with this strategy are that the company granting the license has to give its foreign partner access to its technological know-how and so risks losing control over its secrets.

franchising Selling to a foreign organization the rights to use a brand name and operating know-how in return for a lump-sum payment and a share of the profits.

Whereas licensing is pursued primarily by manufacturing companies, franchising is pursued primarily by service organizations. In **franchising**, a company (the franchiser) sells to a foreign organization (the franchisee) the rights to use its brand name and operating know-how in return for a lump-sum payment and share of the franchiser's profits. Hilton Hotels might sell a franchise to a local company in Chile to operate hotels under the Hilton name in return for a franchise payment. The advantage of franchising is that the franchiser does not have to bear the development costs of overseas expansion and avoids the many problems associated with setting up foreign operations. The downside is that the organization that grants the

franchise may lose control over the way in which the franchisee operates and product quality may fall. In this way, franchisers such as Hilton, Avis, and McDonald's risk losing their good names. American customers who buy McDonald's hamburgers in Korea may reasonably expect those burgers to be as good as the ones they get at home. If they are not, McDonald's reputation will suffer over time. Once again, the Internet facilitates communication between partners and allows them to better meet each other's expectations.

strategic alliance

An agreement in which managers pool or share their organization's resources and know-how with a foreign company, and the two organizations share the rewards and risks of starting a new venture.

joint venture

A strategic alliance among two or more companies that agree to jointly establish and share the ownership of a new business.

wholly owned foreign subsidiary

Production operations established in a foreign country independent of any local direct involvement.

STRATEGIC ALLIANCES One way to overcome the loss-of-control problems associated with exporting, licensing, and franchising is to expand globally by means of a strategic alliance. In a **strategic alliance**, managers pool or share their organization's resources and know-how with those of a foreign company, and the two organizations share the rewards or risks of starting a new venture in a foreign country. Sharing resources allows a U.S. company, for example, to take advantage of the high-quality skills of foreign manufacturers and the specialized knowledge of foreign managers about the needs of local customers and to reduce the risks involved in a venture. At the same time, the terms of the alliance give the U.S. company more control over how the good or service is produced or sold in the foreign country than it would have as a franchiser or licenser.

A strategic alliance can take the form of a written contract between two or more companies to exchange resources, or it can result in the creation of a new organization. A **joint venture** is a strategic alliance among two or more companies that agree to jointly establish and share the ownership of a new business.⁴³ An organization's level of involvement abroad increases in a joint venture because the alliance normally involves a capital investment in production facilities abroad in order to produce goods or services outside the home country. Risk, however, is reduced. The Internet and global teleconferencing provide the increased communication and coordination necessary for partners to work together on a global basis. In 2001, for example, Coca-Cola and Nestlé announced that they would form a joint venture and cooperate in marketing their teas, coffees, and health-oriented beverages to more than 50 countries in the world.⁴⁴ Similarly, BP Amoco and Italy's ENI announced that they would form a joint venture to build a \$2.5 billion gas-liquefaction plant in Egypt.⁴⁵

WHOLLY OWNED FOREIGN SUBSIDIARIES When managers decide to establish a **wholly owned foreign subsidiary**, they invest in establishing production operations in a foreign country independent of any local direct involvement. Many Japanese car component companies, for example, have established their own operations in the United States to supply U.S.-based Japanese carmakers such as Toyota and Honda with high-quality components.

Operating alone, without any direct involvement from foreign companies, an organization receives all of the rewards and bears all of the risks associated with operating abroad.⁴⁶ This method of international expansion is much more expensive than the others because it requires a higher level of foreign investment and presents managers with many more threats. However, investment in a foreign subsidiary or division offers significant advantages: It gives an organization high potential returns because the organization does not have to share its profits with a foreign organization, and it reduces the level of risk because the organization's managers have full control over all aspects of their foreign subsidiary's operations.

Moreover, this type of investment allows managers to protect their technology and know-how from foreign organizations. Large, well-known companies like Du Pont, General Motors, Arthur Andersen, and Gillette, which have plenty of resources, make extensive use of wholly owned subsidiaries. No matter what means they choose to expand globally, however, companies have to be careful to design and select the right kind of information systems and Web sites to allow customers to buy their products.

Vertical integration

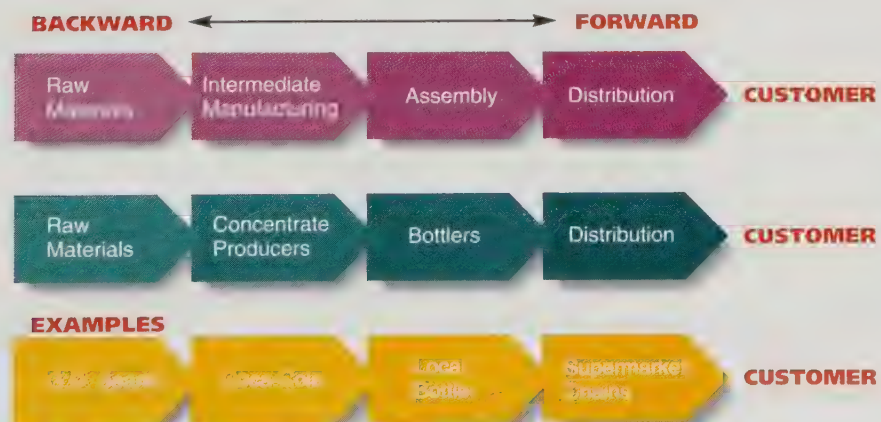
When an organization is doing well in its business, managers often see new opportunities to create value by either producing their own inputs or distributing their own outputs. Managers at E. & J. Gallo Winery, for example, realized that they could lower Gallo's costs if the company produced its own wine bottles rather than buying them from a glass company. As a result, Gallo established a new division to produce glass bottles.

vertical integration A strategy that allows an organization to create value by producing its own inputs or distributing and selling its own outputs.

Vertical integration is the corporate-level strategy through which an organization becomes involved in producing its own inputs (*backward* vertical integration) or distributing and selling its own outputs (*forward* vertical integration).⁴⁷ A steel company that supplies its iron ore needs from company-owned iron ore mines is engaging in backward vertical integration. A personal computer company that sells its computers through company-owned distribution outlets, as Tandy did through its Radio Shack stores, is engaging in forward vertical integration.

Figure 6.7 illustrates the four main stages in a typical raw-material-to-consumer value chain; value is added at each stage. Typically, the primary operations of an organization take place in one of these stages. For a company based in the assembly stage, backward integration would involve establishing a new division in intermediate manufacturing or raw-material production, and forward integration would involve establishing a new division to distribute its products to wholesalers or to sell directly to customers. A division at one stage receives the product produced by the division in the previous stage, transforms it in some way—adding value—and then transfers the output at a higher price to the division at the next stage in the chain.

Figure 6.7
Stages in a
Vertical Value
Chain



As an example of how the value chain works, consider the cola segment of the soft-drink industry. Raw-material suppliers include sugar companies and G. D. Searle, manufacturer of the artificial sweetener NutraSweet, which is used in diet colas. These companies sell their products to companies that make concentrate—such as Coca-Cola and PepsiCo—which mix these inputs with others to produce the cola concentrate that they market. In the process, they add value to these inputs. The concentrate producers then sell the concentrate to bottlers, who add carbonated water to the concentrate and package the resulting drink—again adding value to the concentrate. Next, the bottlers sell the packaged product to various distributors, including retail stores such as Costco and Wal-Mart and fast-food chains such as McDonald's. These distributors add value by making the product accessible to customers. Thus, value is added by companies at each stage in the raw-material-to-consumer chain.

A major reason why managers pursue vertical integration is that it allows them either to add value to their products by making them special or unique or to lower the costs of value creation. For example, Coca-Cola and PepsiCo, in a case of forward vertical integration to build brand loyalty and enhance the differentiated appeal of their colas, decided to buy up their major bottlers to increase control over marketing and promotion efforts, which had been handled by the bottlers.⁴⁸ An example of using forward vertical integration to lower costs is Matsushita's decision to open company-owned stores to sell its Panasonic and JVC products and thus keep the profit that otherwise would be earned by independent retailers.⁴⁹

Although vertical integration can help an organization to grow rapidly, it can be a problem when forces in the environment counter the strategies of the organization and make it necessary for managers to reorganize or retrench. Vertical integration can reduce an organization's flexibility to respond to changing environmental conditions. For example, IBM used to produce most of its own components for mainframe computers. While this made sense in the 1970s, it became a major handicap for the company in the fast-changing computer industry of the 1990s. The rise of organizationwide networks of personal computers meant slumping demand for mainframes. As demand fell, IBM found itself with an excess-capacity problem, not only in its mainframe assembly operations but also in component operations. Closing down this capacity cost IBM over \$5 billion.⁵⁰

When considering vertical integration as a strategy to add value, managers must be careful because sometimes vertical integration actually reduces an organization's ability to create value when the environment changes. This is why so many companies now outsource the production of component parts to other companies. IBM, however, found a new opportunity for forward vertical integration in the 1990s.⁵¹ It decided to provide IT consulting services to mainframe users and to advise them on how to install and manage any software packages they chose on their mainframes. Providing such IT services was so profitable for IBM that by 2000 it had recovered its market position.

Formulating Business-Level Strategies

Michael Porter, the researcher who developed the five forces model discussed earlier, also formulated a theory of how managers can select a business-level strategy, a plan to gain a competitive advantage in a particular market or industry.⁵² According to Porter, managers must choose between the two basic ways of increasing the

Table 6.2
Porter's Business-Level Strategies

Strategy	Number of Market Segments Served	
	Many	Few
Low cost	✓	
Focused low cost		✓
Differentiation	✓	
Focused differentiation		✓

value of an organization's products: differentiating the product to add value or lowering the costs of value creation. Porter also argues that managers must choose between serving the whole market or serving just one segment or part of a market. Based on those choices, managers choose to pursue one of four business-level strategies: low cost, differentiation, focused low cost, or focused differentiation (see Table 6.2).

Low-cost strategy

low-cost strategy

Driving the organization's costs down below the costs of its rivals.

With a **low-cost strategy**, managers try to gain a competitive advantage by focusing the energy of all the organization's departments or functions on driving the organization's costs down below the costs of its rivals. This strategy, for example, would require that manufacturing managers search for new ways to reduce production costs, R&D managers focus on developing new products that can be manufactured more cheaply, and marketing managers find ways to lower the costs of attracting customers. According to Porter, organizations pursuing a low-cost strategy can sell a product for less than their rivals sell it and yet still make a profit because of their lower costs. Thus, organizations that pursue a low-cost strategy hope to enjoy a competitive advantage based on their low prices. For example, BIC pursues a low-cost strategy; it offers customers razor blades priced lower than Gillette's and ball-point pens less expensive than those offered by Cross or Waterford.

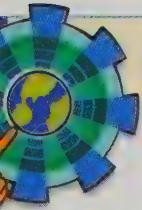
Differentiation strategy

differentiation strategy

Distinguishing an organization's products from the products of competitors in dimensions such as product design, quality, or after-sales service.

With a **differentiation strategy**, managers try to gain a competitive advantage by focusing all the energies of the organization's departments or functions on distinguishing the organization's products from those of competitors on one or more important dimensions, such as product design, quality, or after-sales service and support. Often, the process of making products unique and different is expensive. This strategy, for example, often requires that managers increase spending on product design or R&D to differentiate the product, and costs rise as a result. Organizations that successfully pursue a differentiation strategy may be able to charge a *premium price* for their products, a price usually much higher than the price charged by a low-cost organization. The premium price allows organizations pursuing a differentiation strategy to recoup their higher costs. Coca-Cola,

PepsiCo, and Procter & Gamble are some of the many well-known companies that pursue a strategy of differentiation. They spend enormous amounts of money on advertising to differentiate, and create a unique image for, their products. However, just because companies can differentiate their products does not mean that there cannot be intense competition between them, as the following “Managing Globally” suggests.



Managing Globally

Strategy in the World Package Delivery Business

In 1971, Federal Express (FedEx) turned the package delivery world upside down when it began to offer overnight package delivery by air. Its founder, Fred Smith, had seen the opportunity for next-day delivery because both the U.S. Postal Service and United Parcel Service (UPS) were, at that time, taking several days to deliver packages. Smith was convinced there was pent-up demand for overnight delivery, and he was also convinced that customers would be willing to pay a high premium price to get such a unique new service, at least \$15 a package at that time.⁵³ Smith was right; customers were willing to pay high prices for fast reliable delivery. By discovering and tapping into an unmet customer need, he redefined the package delivery industry.

Several companies imitated FedEx's new strategy and introduced their own air overnight service. None, however, could match FedEx's state-of-the-art information system that allowed continuous tracking of all packages in transit. Several of its competitors went out of business. A few, like Airborne Express, managed to survive by focusing or *specializing* on serving the needs of *one* particular group of customers—corporate customers—and by offering lower prices than FedEx.



FedEx's purchase of Kinko's will allow it to reach more customers by making each Kinko's store a base for its operations.

The well-known road delivery package company UPS initiated an overnight air delivery service of its own in 1998.⁵⁴ UPS managers realized that the future of package delivery lay both on the road and in the air because different customer groups, with different needs, were emerging. It began to aggressively imitate FedEx's state-of-the-art operating and information systems, especially its tracking system. Slowly and surely UPS increased the number of overnight packages that it was delivering. In 1999, UPS announced two major innovations. First, it introduced a new tracking and shipping information system that matched, and even exceeded, the sophistication of the FedEx tracking system because it could work with *any* IT system used by corporate customers. (By contrast, customers had to install and use FedEx's proprietary

IT, an approach that caused more work and cost for them.) Second, UPS integrated its overnight air service into its nationwide delivery service and created a seamless interface between these two different aspects of its business. This has given it a differentiation advantage over FedEx because UPS can deliver short-range and mid-distance packages, those being shipped within about 500 miles, more quickly than FedEx, as well as match the speed and reliability of FedEx's long-range operations.

Competition between FedEx and UPS became intense in the early 2000s. Then, in 2003, both companies received a shock when the largest global package delivery company, DHL, announced that it would purchase Airborne Express and would thus become a direct competitor of FedEx and UPS. Soon, when DHL began a marketing campaign to emphasize the extent of its global reach and the speed of its operations, all three companies started to fight for customers and find new ways of differentiating their products. In 2003 FedEx announced that it would purchase Kinko's Copies and make each Kinko's store a base for its delivery operations. In doing so, it was following UPS's approach; UPS had purchased a chain of packaging stores and turned them into UPS stores. The fight is ongoing and which company will turn out to be the global leader is still unclear.

“Stuck in the middle”

According to Porter's theory, managers cannot simultaneously pursue both a low-cost strategy and a differentiation strategy. Porter identified a simple correlation: Differentiation raises costs and thus necessitates premium pricing to recoup those high costs. For example, if BIC suddenly began to advertise heavily to try to build a strong global brand image for its products, BIC's costs would rise. BIC then could no longer make a profit simply by pricing its blades or pens lower than Gillette or Cross. According to Porter, managers must choose between a low-cost strategy and a differentiation strategy. He refers to managers and organizations that have not made this choice as being “stuck in the middle.”

According to Porter, organizations stuck in the middle tend to have lower levels of performance than do those that pursue a low-cost or a differentiation strategy. To avoid being stuck in the middle, top managers must instruct departmental managers to take actions that will result in either low cost or differentiation.

However, exceptions to this rule can be found. In many organizations managers have been able to drive costs below those of rivals and simultaneously differentiate their products from those offered by rivals.⁵⁵ For example, Toyota's production system is reportedly the most efficient in the world. This efficiency gives Toyota a low-cost strategy vis-à-vis its rivals in the global car industry. At the same time, Toyota has differentiated its cars from those of rivals on the basis of superior design and quality. This superiority allows the company to charge a premium price for many of its popular models.⁵⁶ Thus, Toyota seems to be simultaneously pursuing both a low-cost and a differentiated business-level strategy. This example suggests that although Porter's ideas may be valid in most cases, very well managed companies

such as Toyota, McDonald's, and Dell Computer may have both low costs and differentiated products.

Focused low-cost and focused differentiation strategies

focused low-cost strategy Serving only one segment of the overall market and being the lowest-cost organization serving that segment.

focused differentiation strategy Serving only one segment of the overall market and trying to be the most differentiated organization serving that segment.

Both the differentiation strategy and the low-cost strategy are aimed at serving many or most segments of a particular market, such as for cars or computers. Porter identified two other business-level strategies that aim to serve the needs of customers in only one or a few market segments.⁵⁷ Managers pursuing a **focused low-cost strategy** serve one or a few segments of the overall market and aim to make their organization the lowest-cost company serving that segment. For example, Cott Corporation is the world's leading supplier of *retailer* brand-name carbonated soft drinks. With production facilities in Canada, the United States, and the United Kingdom, Cott produces, packages, and distributes a wide selection of retailer-brand beverages for grocery, mass-merchandise, drugstore, and convenience store chains. For example, all Wal-Mart soda sold under the Sam's brand name is made by Cott. However, note that while Cott is the world's leading supplier of *retailer-brand-name* sodas, it is focusing on a low-cost strategy. It makes no attempt to compete with Coke and Pepsi, which, pursue a differentiation strategy and whose brand-name sodas dominate the global soda market.

By contrast, managers pursuing a **focused differentiation strategy** serve just one or a few segments of the market and aim to make their organization the most differentiated company serving that segment. BMW, for example, pursues a focused strategy, producing cars exclusively for higher-income customers. By contrast, Toyota pursues a differentiation strategy and produces cars that appeal to consumers in almost all segments of the car market, from basic transportation (Toyota Tercel), through the middle of the market (Toyota Camry), to the high-income end of the market (Lexus). L. L. Bean, discussed in the opening case, also is pursuing this strategy; it targets customers who want to buy high-quality sporting products.

As these examples suggest, companies pursuing either of these focused strategies have chosen to *specialize* in some way by directing their efforts at a particular kind of customer (such as serving the needs of babies or affluent customers) or even the needs of customers in a specific geographic region (customers on the East or West Coast).

Zara, a Spanish manufacturer of fashionable clothing, provides an excellent example of how a company can pursue both a low-cost and a differentiated focused strategy at the same time by using new information technologies. Well-known fashion houses like Channel, Dior, and Armani can charge thousands of dollars for the fashionable collections of suits and dresses that they introduce twice yearly in the fall and in the spring. Only the very rich can afford such differentiated and expensive clothing, and this has opened up a gap in the fashion market for companies that can supply fashionable clothes at lower prices. Essentially, these companies have the capabilities to pursue a focused differentiation and cost-leadership strategy.

While many clothing companies, such as the United States' The Gap, Sweden's Hennes & Mauritz, and England's Jaeger and Laura Ashley, have attempted to

supply fashionable clothes at lower prices, none has succeeded as well as Spanish clothes maker Zara, whose sales have soared in recent years.⁵⁸ Zara has managed to position itself as the low-price/cost leader in the fashion segment of the clothing market because of the way it uses information technology. It has created an information system that allows it to manage its design and manufacturing process in a way that minimizes the inventory it has to carry—the major cost borne by a clothing retailer. However, its IT also gives instantaneous feedback on which clothes are selling well and in which countries, and this gives it a competitive advantage from differentiation. Specifically, Zara can manufacture more of a particular kind of dress or suit to meet high customer demand, decide which clothing should be sold in its rapidly expanding network of global stores, and constantly change the mix of clothes it offers customers to keep up with fashion. Moreover, it can do this at relatively small output levels, something which is also a part of a specialized, focused strategy.

Zara's IT also allows it to manage the interface between its design and manufacturing operations more efficiently. Zara only takes five weeks to design a new collection and then a week to make it. Other fashion houses, by contrast, can take six or more months to design the collection and then three more before it is available in stores.⁵⁹ This short time to market gives Zara great flexibility and allows the company to respond quickly to the rapidly changing fashion market in which fashions can change several times a year. Because of the quick manufacturing-to-sales cycle and just-in-time fashion, Zara offers its clothes collections at relatively low prices and still makes profits that are the envy of the fashion clothing industry.⁶⁰

Formulating Functional-Level Strategies

functional-level strategy A plan that indicates how a function intends to achieve its goals.

Zara has developed many kinds of strengths in functions such as clothing design and IT that have given it a competitive advantage. **Functional-level strategy** is a plan of action to improve the ability of an organization's functions to create value. It is concerned with the actions that managers of individual functions (such as manufacturing

or marketing) can take to add value to an organization's goods and services and thereby increase the value customers receive. The price that customers are prepared to pay for a product indicates how much they value an organization's products. The more customers value a product, the more they are willing to pay for it.

There are two ways in which functions can add value to an organization's products:

1. Functional managers can lower the costs of creating value so that an organization can attract customers by keeping its prices lower than its competitors' prices.
2. Functional managers can add value to a product by finding ways to differentiate it from the products of other companies.

If customers see more value in one organization's products than in the products of its competitors, they may be willing to pay premium prices. Thus, there must be a fit between functional- and business-level strategies if an organization is to achieve its mission and goal of maximizing the amount of value it gives customers. The better the fit between functional- and business-level strategies, the greater will be the

Table 6.3

How Functions Can Lower the Costs and Create Value or Add Value to Create a Competitive Advantage

Value-Creating Function	Ways to Lower the Cost of Creating Value (Low-Cost Advantage)	Ways to Add Value (Differentiation Advantage)
Sales and marketing Materials management Research and development Manufacturing Human resources management	<ul style="list-style-type: none"> • Find new customers • Find low-cost advertising methods • Use just-in-time inventory system/computerized warehousing • Develop long-term relationships with suppliers and customers • Improve efficiency of machinery and equipment • Design products that can be made more cheaply • Develop skills in low-cost manufacturing • Reduce turnover and absenteeism • Raise employee skills 	<ul style="list-style-type: none"> • Promote brand-name awareness and loyalty • Tailor products to suit customers' needs • Develop long-term relationships with suppliers to provide high-quality inputs • Reduce shipping time to customers • Create new products • Improve existing products • Increase product quality and reliability • Hire highly skilled employees • Develop innovative training programs

organization's competitive advantage—its ability to attract customers and the revenue they provide.

Each organizational function has an important role to play in the process of lowering costs or adding value to a product (see Table 6.3, page 232). Manufacturing can find new ways to lower production costs or to build superior quality into the product to add value. Marketing, sales, and after-sales service and support can add value by, for example, building brand loyalty (as Coca-Cola and PepsiCo have done in the soft-drink industry) and finding more effective ways to attract customers. Human resource management can lower the costs of creating value by recruiting and training a highly productive workforce. The R&D function can lower the costs of creating value by developing more efficient production processes. Similarly, R&D can add value by developing new and improved products that customers value over established product offerings.

Creating value at the functional level requires the adoption of many state-of-the-art management techniques and practices that are discussed at length in the following chapter. We will just note here that it is the responsibility of managers at the functional level to identify these techniques and develop a functional-level plan that contains the strategies necessary to develop them. The important issue to remember is that all of these techniques can help an organization achieve a competitive advantage by lowering the costs of creating value or by adding value above and beyond that offered by rivals.

Planning and Implementing Strategy

After identifying appropriate strategies to attain an organization's mission and goals, managers confront the challenge of putting those strategies into action. Strategy implementation is a five-step process:

1. Allocate responsibility for implementation to the appropriate individuals or groups.
2. Draft detailed action plans that specify how a strategy is to be implemented.
3. Establish a timetable for implementation that includes precise, measurable goals linked to the attainment of the action plan.
4. Allocate appropriate resources to the responsible individuals or groups.
5. Hold specific individuals or groups responsible for the attainment of corporate, divisional, and functional goals.

The planning process goes beyond the mere identification of strategies; it also includes actions taken to ensure that the organization actually puts its strategies into action. It should be noted that the plan for implementing a strategy might require radical redesign of the structure of the organization, the development of new control systems, and the adoption of a program for changing the culture of the organization. These are all issues that we address in the next three chapters.

Summary and Review

PLANNING Planning is a three-step process: (1) determining an organization's mission and goals; (2) formulating strategy; (3) implementing strategy. Managers use planning to identify and select appropriate goals and courses of action for an organization and to decide how to allocate the resources they need to attain those goals and carry out those actions. A good plan builds commitment for the organization's goals, gives the organization a sense of direction and purpose, coordinates the different functions and divisions of the organization, and controls managers by making them accountable for specific goals. In large organizations planning takes place at three levels: corporate, business or divisional, and functional or departmental. Although planning is typically the responsibility of a well-defined group of managers, the subordinates of those managers should be given every opportunity to have input into the process and to shape the outcome. Long-term plans have a time horizon of five years or more; intermediate-term plans, between one and five years; and short-term plans, one year or less.

DETERMINING MISSION AND GOALS AND FORMULATING STRATEGY Determining the organization's mission requires that managers define the business of the organization and establish major goals. Strategy formulation requires that managers perform a SWOT analysis and then choose appropriate strategies at the corporate, business, and functional levels. At the corporate level, organizations use strategies such as concentration on a single business, diversification, international expansion, and vertical integration to help increase the value of the goods and services provided to customers. At the business level, managers are responsible for developing a successful low-cost or differentiation strategy, either

for the whole market or for a particular segment of it. At the functional level, departmental managers strive to develop and use their skills to help the organization either to add value to its products by differentiating them or to lower the costs of value creation.

IMPLEMENTING STRATEGY Strategy implementation requires that managers allocate responsibilities to appropriate individuals or groups, draft detailed action plans that specify how a strategy is to be implemented, establish a timetable for implementation that includes precise, measurable goals linked to the attainment of the action plan, allocate appropriate resources to the responsible individuals or groups, and hold individuals or groups accountable for the attainment of goals.



Management in Action

Topics for Discussion and Action

Discussion

1. Describe the three steps of planning. Explain how they are related.
2. How can scenario planning help managers predict the future?
3. What is the role of divisional and functional managers in the formulation of strategy?
4. Why is it important for functional managers to have a clear grasp of the organization's mission when developing strategies within their departments?
5. What is the relationship among corporate-, business-, and functional-level strategies, and how do they create value for an organization?

Action

6. Ask a manager about the kinds of planning exercises he or she regularly uses. What are the purposes of these exercises, and what are their advantages or disadvantages?
7. Ask a manager to identify the corporate-, business-, and functional-level strategies used by his or her organization.



Building Management Skills

How to Analyze a Company's Strategy

Pick a well-known business organization that has received recent press coverage and for which you can get the annual reports or 10K filings from your school library for a number of years. For this organization, do the following:

1. From the annual reports or 10K filings identify the main strategies pursued by the company over a 10-year period.
2. Try to identify why the company pursued these strategies. What reason was given in the annual reports, press reports, and so on?
3. Document whether and when any major changes in the strategy of the organization occurred. If changes did occur, try to identify the reason for them.
4. If changes in strategy occurred, try to determine the extent to which they were the result of long-term plans and the extent to which they were responses to unforeseen changes in the company's task environment.
5. What is the main industry that the company competes in?
6. What business-level strategy does the company seem to be pursuing in this industry?
7. What is the company's reputation with regard to productivity, quality, innovation, and responsiveness to customers in this industry? If the company has attained an advantage in any of these areas, how has it done so?
8. What is the current corporate-level strategy of the company? What is the company's stated reason for pursuing this strategy?
9. Has the company expanded internationally? If it has, identify its largest international market. How did the company enter this market? Did its mode of entry change over time?





Small Group Breakout Exercise

Low Cost or Differentiation?

Form groups of three or four people, and appoint one member as spokesperson who will communicate your findings to the class when called on by the instructor. Then discuss the following scenario.

You are a team of managers of a major national clothing chain, and you have been charged with finding a way to restore your organization's competitive advantage. Recently, your organization has been experiencing increasing competition from two sources. First, discount stores such as Wal-Mart and Target have been undercutting your prices because they buy their clothes from low-cost foreign manufacturers while you buy most of yours from high-quality domestic suppliers. Discount stores

have been attracting your customers who buy at the low end of the price range. Second, small boutiques opening in malls provide high-price designer clothing and are attracting your customers at the high end of the market. Your company has become stuck in the middle, and you have to decide what to do: Should you start to buy abroad so that you can lower your prices and begin to pursue a low-cost strategy? Should you focus on the high end of the market and become more of a differentiator?

Or should you try to do both and pursue both a low-cost strategy and a differentiation strategy?

1. Using scenario planning, analyze the pros and cons of each alternative.
2. Think about the various clothing retailers in your local malls and city, and analyze the choices they have made about how to compete with one another along the low-cost and differentiation dimensions.



Be the Manager

A group of investors in your city is considering opening a new upscale supermarket to compete with the major supermarket chains that are currently dominating the city's marketplace. They have called you in to help them determine what kind of upscale supermarket they should open. In other words, how

can they best develop a competitive advantage against existing supermarket chains?

Questions

1. List the supermarket chains in your city, and identify their strengths and weaknesses.
2. What business-level strategies are these supermarkets currently pursuing?
3. What kind of supermarket would do best against the competition? What kind of business-level strategy should it pursue?



Additional Activities on the Build Your Management Skills DVD

- **Test Your Knowledge:**
 - (1) Elements of the Planning Process, (2) SWOT Analysis, (3) Porter's Five Forces, and (4) Levels of Strategy
- **Self-Assessment:** Assessing How Personality Type Impacts Your Goal-Setting Skills

Managing Ethically

A few years ago, IBM announced that it had fired the three top managers of its Argentine division because of their involvement in a scheme to secure a \$250 million contract for IBM to provide and service the computers of one of Argentina's largest state-owned banks. The three executives paid \$14 million of the contract money to a third company, CCR, which paid nearly \$6 million to phantom

companies. This \$6 million was then used to bribe the bank executives who agreed to give IBM the contract.

These bribes are not necessarily illegal under Argentine law. Moreover, the three managers argued that all companies have to pay bribes to get new business contracts and they were not doing anything that managers in other companies were not.

Questions

1. Either by yourself or in a group decide if this business practice of paying bribes is ethical or unethical.
2. Should IBM allow its foreign divisions to pay bribes if all other companies are doing so?
3. If bribery is common in a particular country, what effect would this likely have on the nation's economy and culture?



BusinessWeek

Case in the News

Volkswagen Slips Into Reverse

It has been a rough ride for Bernd Pischetsrieder since the former BMW boss took over as chief executive at Volkswagen in April 2002. VW's share price has fallen nearly 50 percent since then, wiping out \$11 billion in market capitalization as profits plummeted at the \$150 billion company.

On July 23, Pischetsrieder delivered more bad news—a 36 percent net profit drop in the first half of 2004. Profits for all of 2003 were already down by more than half, and just to take even more air out of VW's tires, the boss issued a grim earnings warning for this year. In three years—just half a model life cycle in the auto biz—the world's fourth-largest carmaker has gone from Europe's showcase turnaround to major-league laggard.

What's wrong? Volkswagen's vaunted brand premium—the implicit guarantee of quality and innovation that long allowed it to charge as much as 8 percent more than the competition for mass-market cars—is eroding fast. French, Asian,

and even U.S. rivals are improving quality, bolstering manufacturing efficiency, and besting VW at design. Case in point: The Golf compact lost out in 2003 to the Peugeot 206 as Europe's best-selling car for the second year in a row. The all-new, richly priced Golf is running neck-and-neck with its aging French rival this year. To counter slow sales of its Golf in Europe, VW was forced in January to offer a \$1,500 air-conditioning system for free and hefty dealer rebates on used-car trade-ins. In the United States, meanwhile, VW has slapped a \$3,000 rebate on its aging Passat and joined the 0 percent financing game. U.S. losses are expected to reach \$1.4 billion this year, due to dropping sales and the weak dollar's impact on reported earnings.

Another nasty surprise is in China, which until recently accounted for up to 24 percent of VW's operating profit. In late May, General Motors Corp., keen to dethrone VW as China's market leader, cut prices by 11 percent. VW matched the move. GM's sales doubled in the first half of 2004, while VW's fell 4.2 percent. VW

commanded half the mainland market in 1999; now it controls just over a quarter. Pischetsrieder now expects China sales to grow only 5 percent to 7 percent in 2004, down from over 30 percent in recent years. "Our prime objective is profitability, not maintaining market share," he said in a July 23 conference call with financial analysts and journalists.

What's the way out? Pischetsrieder has launched a cost-savings program called ForMotion aimed at trimming \$2.6 billion over two years, on top of the company's existing effort to squeeze costs by \$1.1 billion a year. The plan seeks to cut \$970 million in purchasing costs, \$600 million in reduced staffing, and \$360 million in restructured sales activities. VW is also beefing up its lucrative auto-finance business by buying a leading Dutch car-leasing company.

More models are coming, too: A souped-up Golf is due later this year, and Passat and Jetta remakes debut in 2004. In China, Pischetsrieder is investing \$6 billion over the next four years and aims to double VW's production capacity, to 1.6 million cars, by 2008. VW is

also introducing fresher models to the Chinese market—the Touareg sport utility, the Phaeton luxury sedan, the Audi A6, and a car that will be expressly designed for China. Pischetsrieder is shifting decision-making from VW's Wolfsburg headquarters to Beijing and sending experienced managers.

Pischetsrieder also has a winner in Audi, VW's \$28 billion-in-revenue premium brand. Strong sales of Audi's luxury A8, the new A6 mid-size sedan, and the hot A3 compact helped drive a 10 percent increase in operating profit, to \$666 million, in the first half of 2004. Audi will introduce the rugged Pike's Peak SUV in 2005.

Cost cuts, new models, new focus, a strong luxury brand: sounds good. So why aren't investors impressed? Analysts who once expected 2004 to be a comeback year now say earnings will remain anemic through 2006. "VW is a huge ship. You can't turn it for miles and miles," says George C. Peterson, president of AutoPacific Inc. in Tustin, Calif.

One problem is that achieving big efficiencies is like shooting at a moving target. Pischetsrieder's cuts will help, but analysts say the effort pales in comparison with the thorough streamlining already achieved at Renault, Peugeot, and Chrysler. Besides, "VW has never faced up to

its fundamental cost problem. It has never faced up to the unions," says John Wormald, a partner at London-based consultant Autopolis.

While rivals retooled, VW dallied. Labor costs at VW's factories are 17.4 percent of revenues, versus a European average of 15 percent, according to a July 27 report by Dresdner Kleinwort Wasserstein. Since closing a plant in Germany is politically impossible, analysts say, Pischetsrieder needs to accelerate cost-cutting dramatically and boost sales while improving plant flexibility. "The group is far from being on a sound recovery path," says Bruno Lapierre, an Exane BNP Paribas analyst, in a July 23 report.

VW has also blundered by neglecting to develop a stable of minivans and SUVs, which make up over 54 percent of industry sales in the United States. So far, VW's only offering is the Touareg SUV. "In the United States, it's playing with one hand behind its back. It has no lineup to match Honda and Toyota," says Peterson. "How did that escape them?"

Slow-Moving Managers

Pischetsrieder, who has a consensus-driven management style, is making little headway against a bureaucracy that is resistant to

change. Insiders say VW's chronically weak management and poor execution were aggravated by the nine-year tenure of former CEO Ferdinand K. Piëch, a brilliant but autocratic engineer. "Of the top 100 managers, 50 are not used to making their own decisions or thinking on their own. They wait for the phone to ring to get their orders. They are used to being told what to do," says an auto-industry expert who is close to the company.

Pischetsrieder has sought to set up more democratic decision-making structures, but many say the pace of change is glacial. "What Pischetsrieder wants to do is right—to transform the organization, processes, and behavior," says one consultant. "The question is whether there is enough time to survive the tough period ahead." Looks like it's time for a radical shift of gears.

Questions

1. What is the source of Volkswagen's problems?
2. What strategies is it adopting to solve these problems?

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Imagine Sony on Steroids

It has been a long wait for Sony Corp. For the past two years, the Japanese electronics giant has been gearing up for the second installment of its *Spider-Man* fran-

chise, the web-slinging superstar that grossed a cool \$403 million at the box office when Tobey Maguire last leapt into theaters in his red leotard. Since then, though, Sony has been a decidedly low-swinging outfit. Sinking sales of its TVs, personal digital devices, and video

recorders zapped earnings last year, which fell by 23.4 percent, to \$851 million, for the fiscal year ended on March 31. Film sales, meanwhile, fell 40 percent, to \$320 million, off its *Spider-Man*-charged year, and music revenues struggled in the face of piracy and dwindling

market share. So any signs of a comeback are welcome at Sony these days, whether they shoot webs or not.

The leading man in the Sony revival story is Sir Howard Stringer, a rumpled 62-year-old Welsh-born executive who has his own mission: to turn Sony's perennially underperforming entertainment unit into an engine for growth, not just an afterthought for a company built on electronic gizmos. And in recent months, Sir Howard has been moving faster than Spider-Man through Times Square.

Stringer has placed his biggest bet—\$5 billion—in a bid to buy Kirk Kerkorian's Metro-Goldwyn-Mayer Inc. studio. That would give Sony Hollywood's largest collection of older movies just as new technologies for offering flicks on demand, over the Internet, and on DVD are taking off. That follows a November 2003 deal he engineered to merge his struggling music company with rival Bertelsmann's BMG unit. If approved by European and U.S. regulators, as expected this year, the merger will give the combined company 25 percent of the market while slicing an estimated \$250 million from overhead. "For a while some of us weren't sure what Howard did at Sony," jokes former Viacom President Frank Biondi. "Now we see that he's remaking the entire operation."

And just in time. Stringer, Sony's vice chairman, is under pressure from Sony CEO Nobuyuki Idei to cut costs by 10 percent, part of an overall corporate mandate to reduce overhead company-wide. At the same time, headquarters expects Stringer to help finally make good on the long-held—but rarely accomplished—goal of using Sony's movies, TV shows, and music to fuel sales of new consumer-electronic formats. Sony

executives would not comment for this story.

For now, Stringer has focused heavily on cost-cutting. Last year, he forced out spendthrift music chief Thomas D. Mottola and installed former NBC President Andrew Lack, a deputy from Stringer's days as head of CBS. Lack slashed more than 1,000 jobs, cutting \$100 million. At Sony's film studio, Stringer ordered more than 500 layoffs and has told film executives to rein in profit-participation that was among the richest in the industry. To add muscle, he brought in Michael Lynton, a turnaround expert who shrank costs at Time Warner Inc.'s international AOL operation. Lynton has been ordered to find more places to cut as he streamlines the often chaotic movie making process.

So far, so good But it's always easier to cut than create. While Sony has been profitable in 9 of 11 quarters, Stringer wants to stabilize earnings by grabbing MGM, which has a more than 4,000-film library that generates \$450 million in cash flow from sales of DVDs and to cable TV. But MGM is still a long shot, in part because he had to jury-rig a financing scheme to reduce the parent company's involvement, bringing in two private equity firms and bidding mostly with debt. MGM now says it is looking at alternatives, which could lead to rich new bids from NBC or Time Warner, both of which are itching to get their hands on the studio.

Another Format Fight

If it does win MGM, Sony intends to combine those films with the 3,500 it currently owns to help push a next-generation DVD technology, called Blu-Ray, that offers films in high-definition. Sony needs the added muscle of a large collection

of films to win over Hollywood, which is holding back, waiting for a competing high-definition DVD pushed by Sony's nemesis Toshiba, with help from Warner Bros. and possibly Microsoft. To promote its own format, Sony intends to start shipping versions of its movies on DVD and Blu-Ray in 2005, according to industry insiders. Sony "knows that getting a library is key to the Next Thing—in this case video-on-demand or the Internet," says DVD pioneer and industry consultant Warren Lieberfarb.

In the meantime, Sony is rolling out entertainment on the Internet through Movielink, an online service it pioneered that is now being operated by five major studios. As for the music business, Sony is hustling to catch up with the likes of Apple Computer Inc.'s iTunes. Last spring, it launched a new online music service called Connect, which has deals with McDonald's Corp. and United Airlines Inc. to offer coupons for songs. It's all part of Stringer's attempt to push the Japanese giant into a fast-consolidating entertainment world before it's too late.

Questions

1. What is Stringer's new business-level strategy for Sony and what steps has he taken to pursue it?
2. What kind of corporate-level strategy is he pursuing to help him increase Sony's performance?
3. Go to the Internet and search for articles about what happened to Sony and Stringer in 2005.

Source: Ronald Grover and Tom Lowry, "Imagine Sony on Steroids." Reprinted from the July 12, 2004, issue of *BusinessWeek* by special permission. Copyright © 2004 by the McGraw-Hill Companies, Inc.

CHAPTER

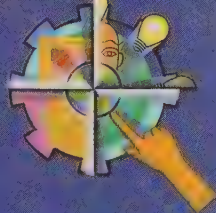
7

Designing Organizational Structure

Learning Objectives

After studying this chapter, you should be able to:

- Identify the factors that influence managers' choice of an organizational structure.
- Explain how managers group tasks into jobs that are motivating and satisfying for employees.
- Describe the types of organizational structures managers can design, and explain why they choose one structure over another.
- Explain why there is a need to both centralize and decentralize authority.
- Explain why managers must coordinate and integrate among jobs, functions, and divisions as an organization grows.
- Explain why managers who seek new ways to increase efficiency and effectiveness are using strategic alliances and network structures.



Management Snapshot

How Three CEOs Worked to Reorganize Lucent

How should managers organize to improve performance?

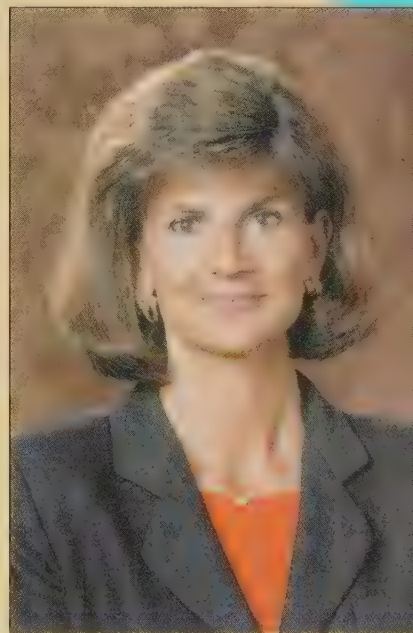
Lucent Technologies, which makes Internet routers and other communications equipment, was one of the high-flying high-tech companies of the 1990s. However, in 2001, Lucent's stock plunged to less than \$7 a share from a high of more than \$70 because of falling sales and mounting losses.¹ The reason? Its managers had backed the development of the wrong kind of router, one based on capacity rather than speed, and speed turned out to be what customers wanted. By contrast, Nortel Networks, one of Lucent's major competitors, had developed fast optical or light-based routers and now had 45 percent of the market compared to Lucent's 15 percent.

Among the many reasons for Lucent's poor decision making was the incredibly complex way it had been organized by its first CEO, Richard McGinn. To promote the speedy development of new products, McGinn had decided that Lucent should be set up as 11 different business divisions, each of which would focus on a particular product and market.²

However, enormous communication and coordination problems arose, since managers in one division did not know what managers in the others were doing. Incompatible kinds of products were being developed, new technology was not being shared across divisions, and it was a nightmare trying to sell Lucent's range of products globally as the 11 business units were each handling their own global sales.

McGinn was forced to leave the company in October 2000. His successor, Henry Schacht, decided efficiency and effectiveness would increase if Lucent reorganized the 11 different divisions into just 5.

This would make managers more accountable for their actions, and they would be



Once again, three's a charm. When Lucent brought in Patricia Russo as its third CEO in as many years, she helped the company return to profitability by implementing a product team structure, improving communications with its research and development arm, Bell Labs.

better able to communicate inside each division. Schacht and his managers spent hundreds of millions of dollars to restructure the company and laid off over 15,000 employees.

By 2001, however, it was clear that Lucent could no longer afford the luxury of having even five divisions because of mounting losses and the need to reduce costs. In July and October, Schacht announced that Lucent would reorganize again both to reduce costs and to allow it to better focus its resources on speeding the new product development process. Another 20,000 employees were laid off (a total of almost one-half of Lucent's employees were laid off as a result of the restructuring). And Lucent announced that it was combining the five units into only two business divisions:³ (1) the Integrated Network Solutions Division, which would handle all Lucent's "land-line" products such as routers, switching, and data software, and (2) the Mobility Solutions Division, which would handle the company's wireless products.

Managers hoped this new structure would perform more flexibly and allow Lucent to respond faster and more effectively to the rapidly changing information technology environment. They also hoped it would save billions of dollars and would be a much more efficient method of organizing. Finally, they

hoped that with just two major divisions it would be far easier to coordinate and manage global sales, something vital if Lucent was to achieve a turnaround.

The reorganization failed, and Lucent's performance continued to deteriorate. Finally, in 2002 Lucent rehired one of its former top managers, Patricia Russo, who had left to join Kodak.⁴ Russo recognized that Lucent's main problems were that each of its two product divisions lacked internal cohesion and that there was still bad communication with Lucent's Bell Labs, where most of its research and development took place. She decided to move to a product team structure to solve Lucent's problems. Now a centralized set of support functions, including Bell Labs and Lucent's marketing and supply chain management, works with each product division to speed product development. In addition, Russo insisted that each product division should break itself into cross-functional teams, each of which would focus on developing new products to compete in a fast-changing environment. As a result of this change, Lucent regained profitability by 2003 and its stock price increased dramatically by 2005, as investors felt that Russo had finally reinvented Lucent and found the right structure.⁵

Overview

As "Management Snapshot" suggests, the challenge facing all three of Lucent's CEOs was to identify the best way to operate in a new, more competitive industry environment. Each CEO was forced to radically change the way they organized their employees and other resources to meet that challenge.

In Part 4 of this book, we examine how managers can organize and control human and other resources to create high-performing organizations. To organize and control (two of the four functions of management identified in Chapter 1), managers must design an organizational architecture that makes the best use of resources to produce the goods and services customers want. **Organizational architecture** is the combination of organizational structure, control systems, culture, and human resource management systems that together determine how efficiently and effectively organizational resources are used.

By the end of this chapter, you will be familiar not only with various organizational structures but also with various factors that determine the organizational design choices that managers make. Then, in Chapter 8, we examine issues surrounding the design of an organization's control systems.

organizational architecture The organizational structure, control systems, culture, and human resource management systems that together determine how efficiently and effectively organizational resources are used.

Designing Organizational Structure

Organizing is the process by which managers establish the structure of working relationships among employees to allow them to achieve organizational goals efficiently and effectively. **Organizational structure** is the formal system of task and job reporting relationships that determines how employees use resources to achieve organizational goals.⁶

Organizational design is the process by which managers make specific organizing choices about tasks and job relationships that result in the construction of a particular organizational structure.⁷

organizational structure A formal system of task and reporting relationships that coordinates and motivates organizational members so that they work together to achieve organizational goals.

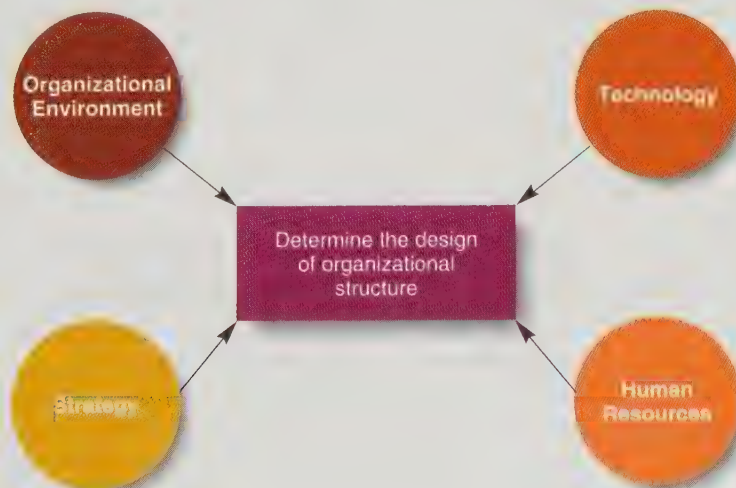
organizational design The process by which managers make specific organizing choices that result in a particular kind of organizational structure.

According to *contingency theory*, managers design organizational structures to fit the factors or circumstances that are affecting the company the most and causing them the most uncertainty.⁸ Thus, there is no one best way to design an organization: Design reflects each organization's specific situation, and researchers have argued that in some situations stable, mechanistic structures may be most appropriate while in others flexible, organic structures might be the most effective. Four factors are important determinants of the type of organizational structure or organizing method managers select: the nature of the organizational environment, the type of strategy the organization pursues, the technology (and particularly *information technology*) the organization uses, and the characteristics of the organization's human resources (see Figure 7.1).⁹

The organizational environment

In general, the more quickly the external environment is changing and the greater the uncertainty within it, the greater are the problems facing managers in trying to gain access to scarce resources. In this situation, to speed decision making and communication and make it easier to obtain resources, managers typically make organizing choices that bring flexibility to the organizational structure.¹⁰ They are likely to decentralize authority and empower lower-level employees to make important operating decisions—a more organic structure. In contrast, if the external environment is stable, resources are readily available, and uncertainty is low, then less coordination and communication among people and functions is needed to

Figure 7.1
Factors Affecting Organizational Structure



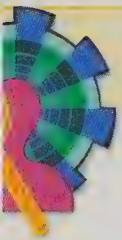
obtain resources, and managers can make organizing choices that bring more stability or formality to the organizational structure. Managers in this situation prefer to make decisions within a clearly defined hierarchy of authority and use extensive rules and standard operating procedures to govern activities—a more mechanistic structure.

As we discussed in Chapter 4, change is rapid in today's marketplace, and increasing competition both at home and abroad is putting greater pressure on managers to attract customers and increase efficiency and effectiveness. Consequently, interest in finding ways to structure organizations—such as through empowerment and self-managed teams—to allow people and departments to behave flexibly has been increasing.

Strategy

As discussed in Chapter 6, once managers decide on a strategy, they must choose the right means of implementing it. Different strategies often call for the use of different organizational structures. For example, a differentiation strategy aimed at increasing the value customers perceive in an organization's goods and services usually succeeds best in a flexible structure; flexibility facilitates a differentiation strategy because managers can develop new or innovative products quickly—an activity that requires extensive cooperation among functions or departments. In contrast, a low-cost strategy that is aimed at driving down costs in all functions usually fares best in a more formal structure, which gives managers greater control over the expenditures and actions of the organization's various departments.¹¹

In addition, at the corporate level, when managers decide to expand the scope of organizational activities by vertical integration or diversification, for example, they need to design a flexible structure to provide sufficient coordination among the different business divisions.¹² As discussed in Chapter 6, many companies have been divesting businesses because managers have been unable to create a competitive advantage to keep them up to speed in fast-changing industries. By moving to a more flexible structure, such as a product division structure, divisional managers gain more control over their different businesses. Finally, expanding internationally and operating in many different countries challenges managers to create organizational structures that allow organizations to be flexible on a global level.¹³ As we discuss later, managers can group their departments or functions and divisions in several ways to allow them to effectively pursue an international strategy, as the story of eMachines and Gateway in the following “Manager as a Person” suggests.



Manager as a Person

Wayne Inouye Has to Restructure Gateway

In 2001, eMachines, a low-price computer maker whose machines sold for less than \$800, was going bankrupt. The main problem? Low product quality because eMachines was organized in a way that led to inefficient manufacturing and ineffective service from its customer service reps, who seemed unable to help customers fix problems with their new computers. Wayne Inouye, a Japanese-American who was previously in charge of Best Buy's computer



Gateway's board of directors was so impressed with Wayne Inouye's success in restructuring eMachines that it decided to acquire the company and hire Inouye as its new CEO.

retailing division, was put in charge of restructuring the company to raise its performance if he could or to shut it down if he could not.

Inouye adopted a radical approach to restructuring eMachines. He decided to outsource the company's manufacturing and sales and customer service operations. Henceforth, eMachines computers would be assembled at low-cost global locations in countries like China or Malaysia, and software specialists in Bangalore, India, would handle its customer service operations. Furthermore, while eMachines used to sell most of its computers online or by advertising, Inouye decided that in the future it would sell its computers through retail partners such as Best Buy.

After outsourcing all these activities, Inouye focused his company's efforts on marketing. Using an IT system that linked eMachines to its retailers, Inouye and his managers had real-time information on which computers were selling and why. With

this information they then redesigned computers and sent the new computer specifications to their overseas manufacturers. In this way, the computers coming off the assembly line matched customers' current needs. The results of all these changes were astounding. By 2003 the company's sales exceeded \$1 billion, and eMachines replaced Gateway to become the number-three global computer maker.

Gateway's board of directors closely monitored eMachines' performance. The success of Inouye's new strategy and structure led them to offer to buy eMachines if Inouye would become the CEO and take charge of merging its operations with Gateway. Inouye accepted. In 2004 he became the CEO of Gateway and restructured the company to raise its performance. His task was to design a new Gateway that would allow it to compete effectively against Dell, the market leader.¹⁴

Technology

Technology is the combination of skills, knowledge, tools, machines, computers, and equipment that are used in the design, production, and distribution of goods and services. As a rule, the more complicated the technology that an organization uses, the more difficult it is for managers and workers to impose strict control on technology or to regulate it efficiently. Thus, the more complicated the technology, the greater is the need for a flexible structure to enhance managers' ability to respond to unexpected situations and give them the freedom to work

out new solutions to the problems they encounter. In contrast, the more routine the technology, the more appropriate is a formal structure, because tasks are simple and the steps needed to produce goods and services have been worked out in advance.

What makes a technology routine or complicated? One researcher who investigated this issue, Charles Perrow, argued that two factors determine how complicated or nonroutine technology is: task variety and task analyzability.¹⁵ *Task variety* is the number of new or unexpected problems or situations that a person or function encounters in performing tasks or jobs. *Task analyzability* is the degree to which programmed solutions are available to people or functions to solve the problems they encounter. Nonroutine or complicated technologies are characterized by high task variety and low task analyzability; this means that many varied problems occur and that solving these problems requires significant nonprogrammed decision making. In contrast, routine technologies are characterized by low task variety and high task analyzability; this means that the problems encountered do not vary much and are easily resolved through programmed decision making.

Examples of nonroutine technology are found in the work of scientists in a research and development laboratory who develop new products or discover new drugs or are seen in the planning exercises an organization's top-management team uses to chart the organization's future strategy. Examples of routine technology include typical mass-production or assembly operations, where workers perform the same task repeatedly and where managers have already identified the programmed solutions necessary to perform a task efficiently. Similarly, in service organizations such as fast-food restaurants, the tasks that crew members perform in making and serving fast food are very routine.

The extent to which the process of actually producing or creating goods and services depends on people or machines is another factor that determines how nonroutine a technology is. The more the technology used to produce goods and services is based on the skills, knowledge, and abilities of people working together on an ongoing basis and not on automated machines that can be programmed in advance, the more complex the technology is. Joan Woodward, a professor who investigated the relationship between technology and organizational structure, differentiated among three kinds of technology on the basis of the relative contribution made by people or machines.¹⁶

Small-batch technology is used to produce small quantities of customized, one-of-a-kind products and is based on the skills of people who work together in small groups. Examples of goods and services produced by small-batch technology include custom-built cars, such as Ferraris and Rolls Royces, highly specialized metals and chemicals that are produced by the pound rather than by the ton, and the process of auditing in which a small team of auditors is sent to a company to evaluate and report on its accounts. Because small-batch goods or services are customized and unique, workers need to respond to each situation as required; thus, a structure that decentralizes authority to employees and allows them to respond flexibly is most appropriate with small-batch technology.

Woodward's second kind of technology, **mass-production technology**, is based primarily on the use of automated machines that are programmed to perform the same operations time and time again. Mass production works most efficiently when each person performs a repetitive task. There is less need for flexibility, and a formal organizational structure is the preferred choice because it gives

small-batch technology

Technology that is used to produce small quantities of customized, one-of-a-kind products and is based on the skills of people who work together in small groups.

mass-production technology

Technology that is based on the use of automated machines that are programmed to perform the same operations over and over.

continuous-process technology

Technology that is almost totally mechanized and is based on the use of automated machines working in sequence and controlled through computers from a central monitoring station.

managers the most control over the production process. Mass production results in an output of large quantities of standardized products such as tin cans, Ford Tauruses, washing machines, and light bulbs, or even services such as a car wash or dry cleaning.

The third kind of technology that Woodward identified, **continuous-process technology**, is almost totally mechanized. Products are produced by automated machines working in sequence and controlled through computers from a central monitoring station. Examples of continuous-process technology include large steel mills, oil refineries, nuclear power stations, and large-scale brewing operations. The role of workers in continuous-process technology is to watch for problems that may occur unexpectedly and cause dangerous or even deadly situations. The possibility of a machinery or computer breakdown, for example, is a major source of uncertainty associated with this technology. If an unexpected situation does occur, employees must be able to respond quickly and appropriately to prevent a disaster from resulting (such as an explosion in a chemical complex). The need for a flexible response makes a flexible organizational structure the preferred choice with this kind of technology.

knowledge

management The sharing and integrating of expertise within and between functions and divisions through real-time, interconnected IT.

INFORMATION TECHNOLOGY As we have seen in previous chapters, new information technologies are having profound effects on the way an organization operates. At the level of organizational structure, IT is changing methods of organizing. IT-enabled organizational structure allows for new kinds of tasks and job reporting relationships among electronically connected people that promote superior communication and coordination. For example, one type of IT-enabled organizational relationship is **knowledge management**, the sharing and integrating of expertise within and between functions and divisions through real-time, interconnected IT.¹⁷ Some benefits from these arrangements include the development of synergies that may result in competitive advantage in the form of product or service differentiation. Unlike the case with more rigid, bureaucratic organizing methods, new IT-enabled organizations can respond more quickly to changing environmental conditions such as increased global competition.

The nature of an organization's technology is an important determinant of its structure. Today, many companies are trying to use IT in innovative ways to make their structures more flexible and to take advantage of the value-creating benefits of complex technology. Many of the ways in which IT affects organizing are discussed in this and later chapters.

Human resources

A final important factor affecting an organization's choice of structure is the characteristics of the human resources it employs. In general, the more highly skilled an organization's workforce is and the more people are required to work together in groups or teams to perform their tasks, the more likely an organization is to use a flexible, decentralized structure. Highly skilled employees or employees who have internalized strong professional values and norms of behavior as part of their training usually desire freedom and autonomy and dislike close supervision. Accountants, for example, have learned the need to report company accounts honestly and impartially, and doctors and nurses have absorbed the obligation to give patients the best care possible.



Highly skilled employees, such as this nurse, have internalized strong professional values and norms of behavior through their education and training. Such employees usually desire freedom and autonomy and dislike close supervision. Flexible structures, characterized by decentralized authority and empowered employees, are well suited to the needs of highly skilled people.

Flexible structures, characterized by decentralized authority and empowered employees, are well suited to the needs of highly skilled people. Similarly, when people work in teams, they must be allowed to interact freely, which also is possible in a flexible organizational structure. Thus, when designing an organizational structure, managers must pay close attention to the workforce and to the work itself.

In summary, an organization's external environment, strategy, technology, and human resources are the factors to be considered by managers in seeking to design the best structure for an organization. The greater the level of uncertainty in the organization's environment, the more complex its strategy and technologies, and the more highly qualified and skilled its workforce, the more likely managers are to design a structure that is flexible and that can change quickly. The more stable the organization's environment, the less complex and more well understood its strategy or technology, and the less skilled its workforce, the more likely managers are to design an organizational structure that is formal and controlling.

How do managers design a structure to be either flexible or formal? The way an organization's structure works depends on the organizing choices managers make about four issues:

- How to group tasks into individual jobs.
- How to group jobs into functions and divisions.
- How to allocate authority in the organization among jobs, functions, and divisions.
- How to coordinate or integrate among jobs, functions, and divisions.

Grouping Tasks into Jobs: Job Design

job design The process by which managers decide how to divide tasks into specific jobs.

The first step in organizational design is **job design**, the process by which managers decide how to divide into specific jobs the tasks that have to be performed to provide customers with goods and services. Managers at McDonald's, for example, have decided how best to divide the tasks required to provide customers with fast, cheap food in each McDonald's restaurant. After experimenting with different McDonald's restaurant. After experimenting with different job arrangements, McDonald's managers decided on a basic division of labor among chefs and food servers. Managers allocated all the tasks involved in actually cooking the food (putting oil in the fat fryers, opening packages of frozen french fries, putting beef patties on the grill, making salads, and so on) to the job of chef. They allocated all the tasks involved in giving the food to customers (such as greeting customers, taking orders, putting fries and burgers into bags, adding salt, pepper, and napkins, and taking money) to food servers. In addition, they created other jobs—the job of dealing with drive-in customers, the job of keeping the restaurant clean, and the job of overseeing employees and responding to unexpected events. The result of the job design process is a *division of labor* among employees, one that McDonald's managers have discovered through experience is most efficient.



At Subway, the role of chef and server is combined into one, making the job “larger” than the jobs of McDonald’s more specialized food servers. The idea behind job enlargement is that increasing the range of tasks performed by the worker will reduce boredom and fatigue. Would you prefer a “larger” job?

Establishing an appropriate division of labor among employees is a critical part of the organizing process, one that is vital to increasing efficiency and effectiveness. At McDonald’s, the tasks associated with chef and food server were split into different jobs because managers found that, for the kind of food McDonald’s serves, this approach was most efficient. It is efficient because when each employee is given fewer tasks to perform (so that each job becomes more specialized), employees become more productive at performing the tasks that constitute each job.

At Subway sandwich shops, however, managers chose a different kind of job design. At Subway, there is no division of labor among the people who make the sandwiches, wrap the sandwiches, give them to customers, and take the money. The roles of chef and food server are combined into one. This different division of tasks and jobs is efficient for Subway and not for McDonald’s because Subway serves a limited menu of mostly submarine-style sandwiches that are prepared to

order. Subway’s production system is far simpler than McDonald’s, because McDonald’s menu is much more varied and its chefs must cook many different kinds of foods.

Managers of every organization must analyze the range of tasks to be performed and then create jobs that best allow the organization to give customers the goods and services they want. In deciding how to assign tasks to individual jobs, however, managers must be careful not to take **job simplification**, the process of reducing the number of tasks that each worker performs, too far.¹⁸ Too much job simplification may reduce efficiency rather than increase it if workers find their simplified jobs boring and monotonous, become demotivated and unhappy, and, as a result, perform at a low level.

job simplification

The process of reducing the number of tasks that each worker performs.

Job enlargement and job enrichment

In an attempt to create a division of labor and design individual jobs to encourage workers to perform at a higher level and be more satisfied with their work, several researchers have proposed ways other than job simplification to group tasks into jobs: job enlargement and job enrichment.

Job enlargement is increasing the number of different tasks in a given job by changing the division of labor.¹⁹ For example, because Subway food servers make the food as well as serve it, their jobs are “larger” than the jobs of McDonald’s food servers. The idea behind job enlargement is that increasing the range of tasks performed by a worker will reduce boredom and fatigue and may increase motivation to perform at a high level—increasing both the quantity and the quality of goods and services provided.

Job enrichment is increasing the degree of responsibility a worker has over a job by, for example, (1) empowering workers to experiment to find new or better ways of doing the job, (2) encouraging workers to develop new skills, (3) allowing workers to decide how to do the work and giving them the responsibility for deciding how to respond to unexpected situations, and (4) allowing workers to monitor

job enlargement

Increasing the number of different tasks in a given job by changing the division of labor.

job enrichment

Increasing the degree of responsibility a worker has over his or her job.

and measure their own performance.²⁰ The idea behind job enrichment is that increasing workers' responsibility increases their involvement in their jobs and thus increases their interest in the quality of the goods they make or the services they provide.

In general, managers who make design choices that increase job enrichment and job enlargement are likely to increase the degree to which people behave flexibly rather than rigidly or mechanically. Narrow, specialized jobs are likely to lead people to behave in predictable ways; workers who perform a variety of tasks and who are allowed and encouraged to discover new and better ways to perform their jobs are likely to act flexibly and creatively. Thus, managers who enlarge and enrich jobs create a flexible organizational structure, and those who simplify jobs create a more formal structure. If workers are grouped into self-managed work teams, the organization is likely to be flexible because team members provide support for each other and can learn from one another.

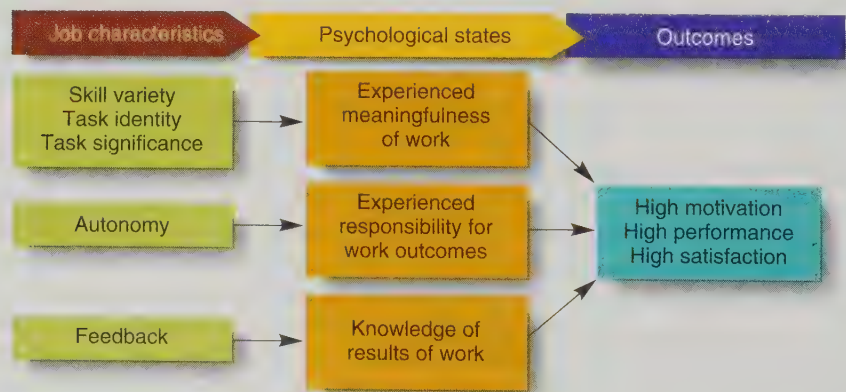
The job characteristics model

J. R. Hackman and G. R. Oldham's job characteristics model is an influential model of job design that explains in detail how managers can make jobs more interesting and motivating.²¹ Hackman and Oldham's model (see Figure 7.2) also describes the likely personal and organizational outcomes that will result from enriched and enlarged jobs.

According to Hackman and Oldham, every job has five characteristics that determine how motivating the job is. These characteristics determine how employees react to their work and lead to outcomes such as high performance and satisfaction and low absenteeism and turnover:

- *Skill variety*—the extent to which a job requires that an employee use a wide range of different skills, abilities, or knowledge. Example: The skill variety required by the job of a research scientist is higher than that called for by the job of a McDonald's food server.
- *Task identity*—the extent to which a job requires that a worker perform all the tasks necessary to complete the job from the beginning to the end of the

Figure 7.2
The Job Characteristics Model



Source: Adapted from J. R. Hackman and G. R. Oldham, *Work Redesign* (Reading, MA: Addison-Wesley, 1980). Reprinted, by permission of Pearson Education, Inc. Upper Saddle River, NJ.

production process. Example: A craftworker who takes a piece of wood and transforms it into a custom-made piece of furniture such as a desk has higher task identity than does a worker who performs only one of the numerous operations required to assemble a television.

- *Task significance*—the degree to which a worker feels his or her job is meaningful because of its effect on people inside the organization such as co-workers or on people outside the organization such as customers. Example: A teacher who sees the effect of his or her efforts in a well-educated and well-adjusted student enjoys high task significance compared to a dishwasher who monotonously washes dishes as they come to the kitchen.
- *Autonomy*—the degree to which a job gives an employee the freedom and discretion needed to schedule different tasks and decide how to carry them out. Example: Salespeople who have to plan their schedules and decide how to allocate their time among different customers have relatively high autonomy compared to assembly-line workers whose actions are determined by the speed of the production line.
- *Feedback*—the extent to which actually doing a job provides a worker with clear and direct information about how well he or she has performed the job. Example: An air traffic controller whose mistakes may result in a midair collision receives immediate feedback on job performance; a person who compiles statistics for a business magazine often has little idea of when he or she makes a mistake or does a particularly good job.

Hackman and Oldham argue that these five job characteristics affect an employee's motivation because they affect three critical psychological states (see Figure 7.2). The more employees feel that their work is *meaningful* and that they are *responsible for work outcomes and responsible for knowing how those outcomes affect others*, the more motivating work becomes and the more likely employees are to be satisfied and to perform at a high level. Moreover, employees who have jobs that are highly motivating are called on to use their skills more and to perform more tasks, and they are given more responsibility for doing the job. All of the foregoing are characteristic of jobs and employees in flexible structures where authority is decentralized and where employees commonly work with others and must learn new skills to complete the range of tasks for which their group is responsible.

Grouping Jobs into Functions and Divisions

Once managers have decided which tasks to allocate to which jobs, they face the next organizing decision: how to group jobs together to best match the needs of the organization's environment, strategy, technology, and human resources. Most top-management teams decide to group jobs into departments and develop a functional structure to use organizational resources. As the organization grows, managers design a divisional structure or a more complex matrix or product team structure.

Choosing a structure and then designing it so that it works as intended is a significant challenge. As noted in Chapter 6, managers reap the rewards of a well-thought-out strategy only if they choose the right type of structure to implement

and execute the strategy. The ability to make the right kinds of organizing choices is often what differentiates effective from ineffective managers.

Functional structure

A *function* is a group of people, working together, who possess similar skills or use the same kind of knowledge, tools, or techniques to perform their jobs. Manufacturing, sales, and research and development are often organized into functional departments. A **functional structure** is an organizational structure composed of all the departments that an organization requires to produce its goods or services. Figure 7.3 (page 252) shows the functional structure that Pier 1 Imports, the home furnishings company, uses to supply its customers with a range of goods from around the world to satisfy their desires for new and innovative products.

Pier 1's main functions are finance and administration, merchandising (purchasing the goods), stores (managing the retail outlets), logistics (managing product

functional structure An organizational structure composed of all the departments that an organization requires to produce its goods or services.

Figure 7.3
The Functional Structure of Pier 1 Imports



distribution), marketing, human resources, and real estate. Each job inside a function exists because it helps the function perform the activities necessary for high organizational performance. Thus, within the logistics department are all the jobs necessary to efficiently distribute and transport products to stores, and inside the marketing department are all the jobs (such as promotion, photography, and visual communication) that are necessary to increase the appeal of Pier 1's products to customers.

There are several advantages to grouping jobs according to function. First, when people who perform similar jobs are grouped together, they can learn from observing one another and thus become more specialized and can perform at a higher level. The tasks associated with one job often are related to the tasks associated with another job, which encourages cooperation within a function. In Pier 1's marketing department, for example, the person designing the photography program for an ad campaign works closely with the person responsible for designing store layouts and with visual communication experts. As a result, Pier 1 is able to develop a strong, focused marketing campaign to differentiate its products.

Second, when people who perform similar jobs are grouped together, it is easier for managers to monitor and evaluate their performance.²² Imagine if marketing experts, purchasing experts, and real-estate experts were grouped together in one function and supervised by a manager from merchandising. Obviously, the merchandising manager would not have the expertise to evaluate all these different people appropriately. However a functional structure allows co-workers to evaluate how well other co-workers are performing their jobs, and if some co-workers are performing poorly, more experienced co-workers can help them develop new skills.

Finally, managers appreciate functional structure because it allows them to create the set of functions they need in order to scan and monitor the competitive environment and obtain information about the way it is changing.²³ With the right set of functions in place, managers are then in a good position to develop a strategy that allows the organization to respond to its changing situation. Employees in marketing can specialize in monitoring new marketing developments that will allow Pier 1 to better target its customers. For example, in 2004 Pier 1 announced that it was firing its current advertising agency and aggressively searching for a new one that could get the company closer to its customers.²⁴ Employees in merchandising can monitor all potential suppliers of home furnishings both at home and abroad to find the goods most likely to appeal to Pier 1's customers and manage Pier 1's global outsourcing supply chain.

As an organization grows, and particularly as its task environment and strategy change because it is beginning to produce a wider range of goods and services for different kinds of customers, several problems can make a functional structure less efficient and effective.²⁵ First, managers in different functions may find it more difficult to communicate and coordinate with one another when they are responsible for several different kinds of products, especially as the organization grows both domestically and internationally. Second, functional managers may become so preoccupied with supervising their own specific departments and achieving their departmental goals that they lose sight of organizational goals. If that happens, organizational effectiveness will suffer because managers will be viewing issues and problems facing the organization only from their own, relatively narrow, departmental perspectives.²⁶ Both of these problems can reduce efficiency and effectiveness.

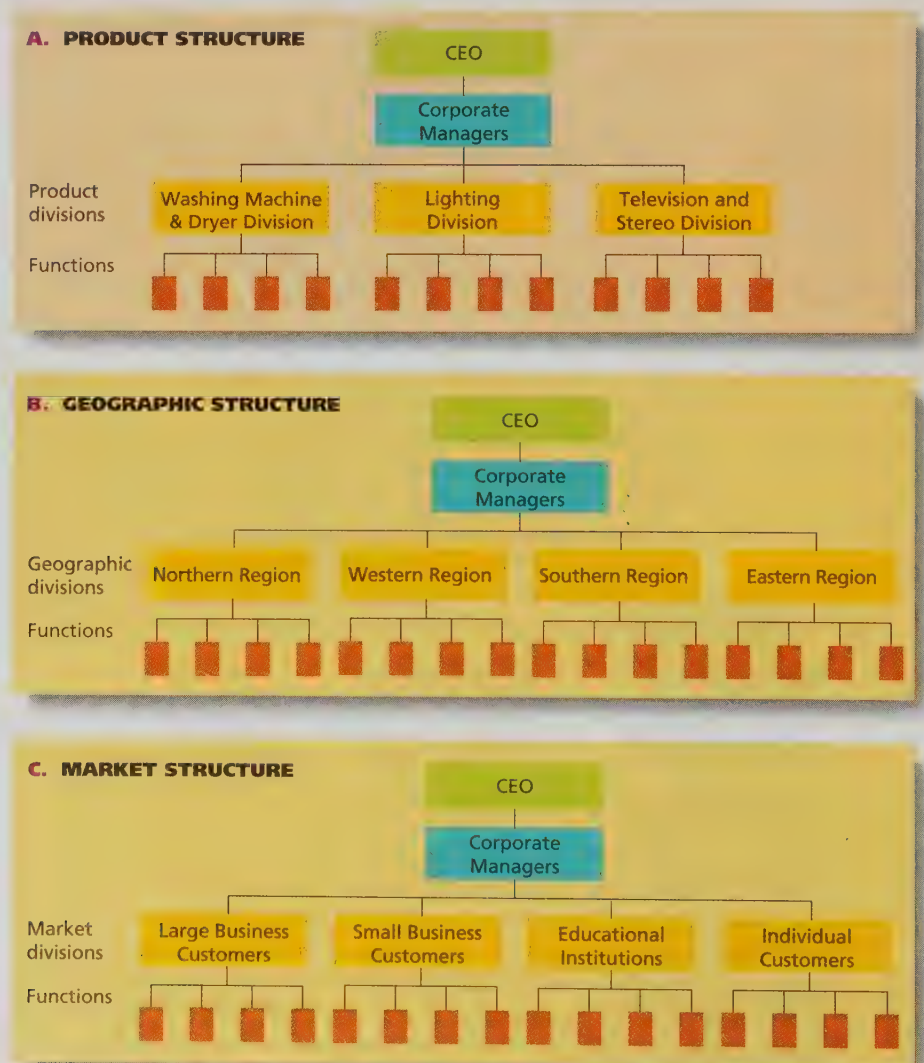
Divisional structures: product, market, and geographic

divisional structure

An organizational structure composed of separate business units within which are the functions that work together to produce a specific product for a specific customer.

As the problems associated with growth and diversification increase over time, managers must search for new ways to organize their activities to overcome the problems associated with a functional structure. Most managers of large organizations choose a **divisional structure** and create a series of business units to produce a specific kind of product for a specific kind of customer. Each *division* is a collection of functions or departments that work together to produce the product. The goal behind the change to a divisional structure is to create smaller, more manageable units within the organization. There are three forms of divisional structure (see Figure 7.4, page 254).²⁷ When managers organize divisions

Figure 7.4
Product, Market, and Geographic Structures



according to the *type of good or service* they provide, they adopt a product structure. When managers organize divisions according to the *area of the country or world* they operate in, they adopt a geographic structure. When managers organize divisions according to the *type of customer* they focus on, they adopt a market structure.

PRODUCT STRUCTURE Imagine the problems that managers at Pier 1 would encounter if they decided to diversify into producing and selling cars, fast food, and health insurance—in addition to home furnishings—and tried to use their existing set of functional managers to oversee the production of all four kinds of products. No manager would have the necessary skills or abilities to oversee those four products. No individual marketing manager, for example, could effectively market cars, fast food, health insurance, and home furnishings at the same time. To perform a functional activity successfully, managers must have experience in specific markets or industries. Consequently, if managers decide to diversify into new industries or to expand their range of products, they commonly design a product structure to organize their operations (see Figure 7.4a).

product structure

An organizational structure in which each product line or business is handled by a self-contained division.

Using a **product structure**, managers place each distinct product line or business in its own self-contained division and give divisional managers the responsibility for devising an appropriate business-level strategy to allow the division to compete effectively in its industry or market.²⁸ Each division is self-contained because it has a complete set of all the functions—marketing, R&D, finance, and so on—that it needs to produce or provide goods or services efficiently and effectively. Functional managers report to divisional managers, and divisional managers report to top or corporate managers.

Grouping functions into divisions focused on particular products has several advantages for managers at all levels in the organization. First, a product structure allows functional managers to specialize in only one product area, so they are able to build expertise and fine-tune their skills in this particular area. Second, each division's managers can become experts in their industry; this expertise helps them choose and develop a business-level strategy to differentiate their products or lower their costs while meeting the needs of customers. Third, a product structure frees corporate managers from the need to supervise directly each division's day-to-day operations; this latitude allows corporate managers to create the best corporate-level strategy to maximize the organization's future growth and ability to create value. Corporate managers are likely to make fewer mistakes about which businesses to diversify into or how to best expand internationally, for example, because they are able to take an organizationwide view.²⁹ Corporate managers also are likely to evaluate better how well divisional managers are doing, and they can intervene and take corrective action as needed.

The extra layer of management, the divisional management layer, can improve the use of organizational resources. Moreover, a product structure puts divisional managers close to their customers and lets them respond quickly and appropriately to the changing task environment. Consider how Viacom, the huge media entertainment company, created a product structure.

Sumner Redstone, the billionaire chairman of Viacom, is continually making acquisitions that add to the range of entertainment products the company provides to its customers. Under Redstone, Viacom started in the cable and television business and expanded into several fields: entertainment, networks and broadcasting, video,

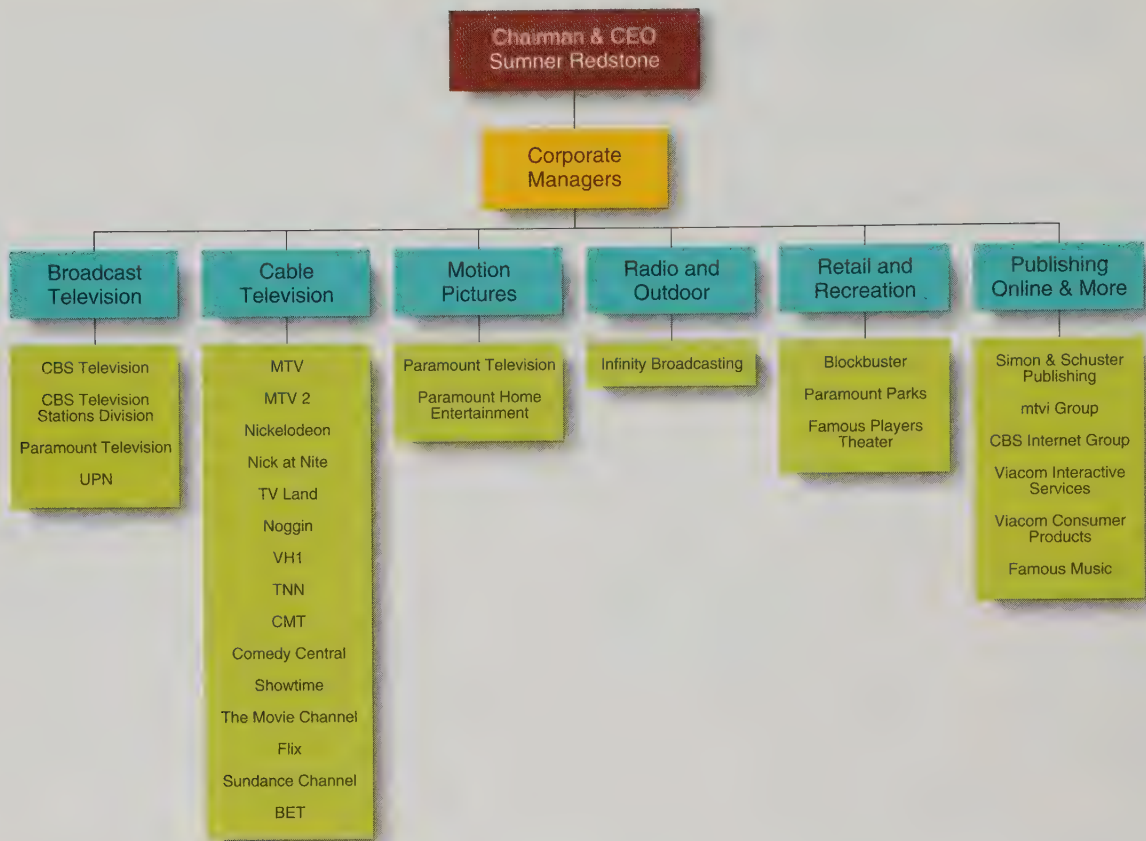


Figure 7.5
Viacom's 2001 Product Structure

music, theme parks, publishing, and television. In 2000, for example, Viacom acquired CBS television and BET.³⁰

To manage Viacom's many different businesses effectively, Redstone decided to design a product structure (see Figure 7.5). He put each business in a separate division and gave managers in each division responsibility for making their business the number-one performer in its industry. Redstone recognized, however, that the different divisions could help each other and create synergies for Viacom by sharing their skills and resources. Blockbuster, for example, could launch a major advertising campaign to publicize the movies that Paramount makes and thus boost the visibility of both divisions' products, and Simon & Schuster could produce and publish specific books to tie in with the opening of a movie and thus boost ticket and book sales. To achieve these synergies, Redstone created a team of corporate managers who are responsible for working with the different divisional managers to identify new opportunities to create value. So far, this method of organizing has served Viacom well, and it has become one of the top-four media and entertainment companies.³¹

A pharmaceutical company that has recently adopted a new product structure to better organize its activities is profiled in the following "Management Insight."

Management Insight

GlaxoSmithKline's New Product Structure

The need to innovate new kinds of prescription drugs in order to boost performance is a continual battle for pharmaceutical companies. In the 2000s, many of these companies have been merging to try to increase their research productivity, and one of them, GlaxoSmithKline, was created from the merger between Glaxo Wellcome and SmithKline Beechum.³² Prior to the merger, both companies experienced a steep decline in the number of new prescription drugs their scientists were able to invent. The problem facing the new company's top managers was how to best use and combine the talents of the scientists and researchers from both of the former companies to allow them to quickly innovate exciting new drugs.

Top managers realized that after the merger there would be enormous problems associated with coordinating the activities of the thousands of research scientists who were working on hundreds of different kinds of drug research programs. Understanding the problems associated with large size, the top managers decided to group the researchers into eight smaller product divisions to allow them to focus on particular clusters of diseases such as heart disease or viral infections. The members of each product division were told that they would be rewarded based on the number of new prescription drugs they were able to invent and the speed with which they could bring these new drugs to the market.

To date, GlaxoSmithKline's new product structure has worked well. The company claimed that by 2004 research productivity had more than doubled since the reorganization. The number of new drugs moving into clinical trials had doubled from 10 to 20, and the company had 148 new drugs that were being tested.³³ Moreover, the company claims that the morale of its researchers has increased and turnover has fallen because the members of each division enjoy working together and collaborating to innovate lifesaving new drugs. The company expects to have the best new drug pipeline in its industry in the next three to four years.

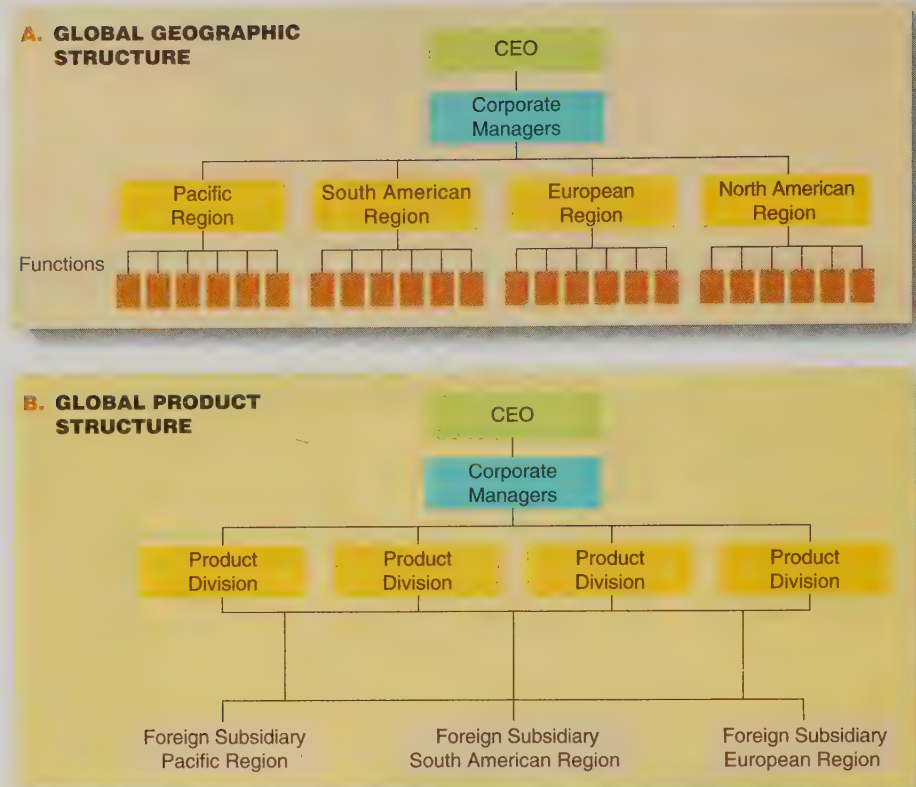


When Glaxo Wellcome and SmithKline Beechum merged, managers resolved the problem of how to coordinate the activities of thousands of research scientists by organizing them into product divisions focusing on clusters of diseases.

geographic structure An organizational structure in which each region of a country or area of the world is served by a self-contained division.

GEOGRAPHIC STRUCTURE When organizations expand rapidly both at home and abroad, functional structures can create special problems because managers in one central location may find it increasingly difficult to deal with the different problems and issues that may arise in each region of a country or area of the world. In these cases, a **geographic structure**, in which divisions are broken down by geographic location, is often chosen (see Figure 7.4b). To achieve the corporate mission of providing next-day mail service, Fred Smith, CEO of Federal Express, chose a geographic structure and divided up operations by creating a division in each region. Large retailers like Macy's, Neiman Marcus, and Brooks Brothers also use a geographic structure. Since the needs of retail customers differ by region—for

Figure 7.6
Global
Geographic
and Global
Product
Structures



example, surfboards in California and down parkas in the Midwest—a geographic structure gives retail regional managers the flexibility they need to choose the range of products that best meets the needs of regional customers.

In adopting a *global geographic structure*, such as shown in Figure 7.6a, managers locate different divisions in each of the world regions where the organization operates. Managers are most likely to do this when they pursue a multidomestic strategy because customer needs vary widely by country or world region. For example, if products that appeal to U.S. customers do not sell in Europe, the Pacific Rim, or South America, then managers must customize the products to meet the needs of customers in those different world regions; a global geographic structure with global divisions will allow them to do this.

In contrast, to the degree that customers abroad are willing to buy the same kind of product, or slight variations thereof, managers are more likely to pursue a global strategy. In this case they are more likely to use a *global product structure*. In a global product structure, each product division, not the country and regional managers, takes responsibility for deciding where to manufacture its products and how to market them in foreign countries worldwide (see Figure 7.6b). Product division managers manage their own global value chains and decide where to establish foreign subsidiaries to distribute and sell their products to customers in foreign countries. As we noted at the beginning of this chapter, an organization's strategy is a major determinant of its structure both at home and abroad. Three companies that have been changing their global structures to increase their performance are profiled in the following "Managing Globally."

Managing Globally

Nokia, Dow, and the LEGO Company Revamp Their Global Structures to Raise Performance

In 2004, suffering from its worst-ever annual losses, caused by a 25 percent decline in global sales, the LEGO company decided it needed to restructure its European operations.³⁹ Until 2004, the LEGO company had operated with three global subdivisions *inside* its European division—central, northern, and southern. Many problems had arisen with this structure. Each subdivision was performing many of the same activities, so the duplication of activities was raising operating costs. The subdivisions often did not cooperate and share information on new product developments or on changes in customer needs. As a result, many opportunities were being lost, especially because this structure made it even more difficult to communicate with the LEGO company's other global divisions, such as its U.S. and Asian divisions.

The LEGO company's solution was to abolish these subdivisions and reorganize them into one European division under the control of LEGO's former top global marketer, Henrik Poulsen.⁴⁰ Poulsen reports to the LEGO company's CEO, just as do the heads of the LEGO company's other global divisions, and the company is hoping that this will lead to an increase in cooperation among its divisions around the world. The goal of the reorganization is to help the LEGO company's global divisions learn from one another and work together to develop toys that better suit the changing needs of customers throughout the world.

While the LEGO company is attempting to increase global sales by combining its three European units into one, in 2004 U.S. giant Dow Chemicals decided that the best way to leverage the skills and resources of its global chemicals division was to split the division into three different global product groups—plastics, chemicals and intermediates, and performance chemicals.⁴¹ Dow believes that when each group acts as a self-contained unit this will make it easier for managers to focus on one range of chemical products that can then be delivered to customers around the world.⁴² Note that to raise performance in Dow's case the issue was to create more product divisions, while the issue facing the LEGO company was to reduce the number of market divisions.



Careful planning was needed in designing this LEGO structure.

Finally, Nokia, the Finnish company that is the world's leader in cellular phones, also made a change to its global structure in 2004. Nokia recognized that it had an important weakness in its product line, wireless business communications, by means of which, for example, a company can stay in touch with its workforce through some form of wireless communication such as laptops, Palm Pilots and other PDAs, or wireless phones that allow employees to share information and communicate with each other.

Since this part of the wireless market is rapidly growing, Nokia chairman Jorma Ollila decided to create a new global division to develop new wireless communication products and a new global product division, the Enterprise Solutions group. Moreover, to give the new divisions the autonomy to develop products quickly, he set them up in New York and appointed a former HP manager, Mary McDowell, to develop an entry technology that will offer everything from server software to handsets and compete with giants like HP and IBM. Since the potential market in this area is expected to grow from \$27 to \$43 billion by 2007, Nokia hopes to obtain a significant share of this lucrative market to help boost its performance.⁴³

market structure

An organizational structure in which each kind of customer is served by a self-contained division; also called *customer structure*.

MARKET STRUCTURE Sometimes the pressing issue facing managers is to group functions according to the type of customer buying the product, in order to tailor the products the organization offers to each customer's unique demands. A computer company like Dell, for example, has several kinds of customers, including large businesses (which might demand networks of computers linked to a main-frame computer), small companies (which may need just a few PCs linked together), educational users in schools and universities (which might want thousands of independent PCs for their students), and individual users (who may want a high-quality multimedia PC so that they can play the latest video games).

To satisfy the needs of diverse customers, a company might adopt a **market structure** (also called a *customer structure*), which groups divisions according to the particular kinds of customers they serve (see Figure 7.4c). A market structure allows managers to be responsive to the needs of their customers and allows them to act flexibly in making decisions in response to customers' changing needs.

Matrix and product team designs

Moving to a product, market, or geographic divisional structure allows managers to respond more quickly and flexibly to the particular set of circumstances they confront. However, when the environment is dynamic and changing rapidly and uncertainty is high, even a divisional structure may not provide managers with enough flexibility to respond to the environment quickly. When customer needs or information technology are changing rapidly and the environment is very uncertain, managers must design the most flexible kind of organizational structure available: a matrix structure or a product team structure (see Figure 7.7).

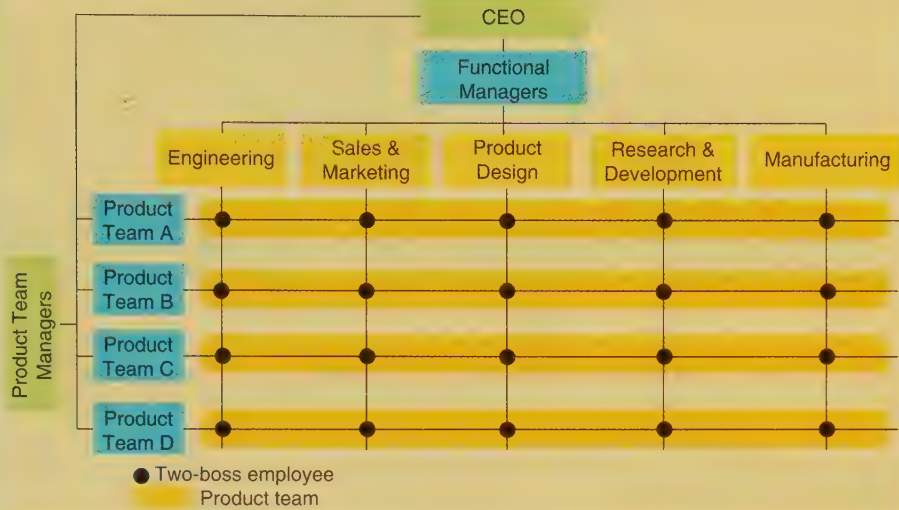
matrix structure

An organizational structure that simultaneously groups people and resources by function and by product.

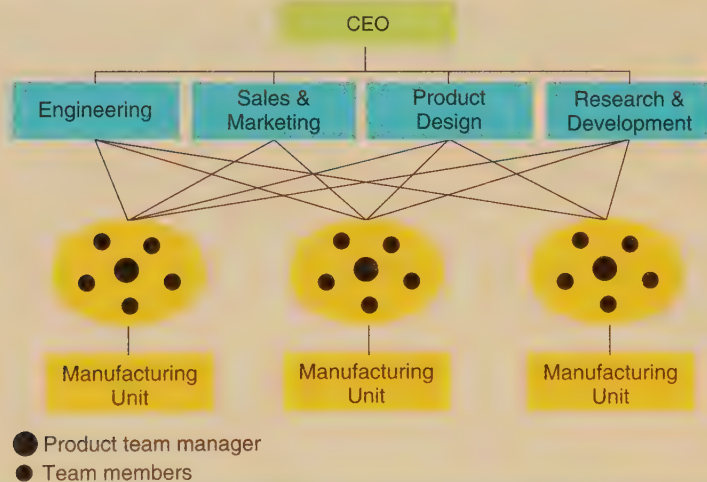
MATRIX STRUCTURE In a **matrix structure**, managers group people and resources in two ways simultaneously: by function and by product.³⁴ Employees are grouped by *functions* to allow them to learn from one another and become more skilled and productive. In addition, employees are grouped into *product teams* in which members of different functions work together to develop a specific product. The result is a complex network of reporting relationships among product teams and functions that makes the matrix structure very flexible (see Figure 7.7a). Each person in a product team reports to two bosses: (1) a functional boss, who assigns individuals to a team and evaluates their performance from a functional perspective, and (2) the boss of the product team, who evaluates their performance on the team. Thus, team members are known as *two-boss employees* because they report to two managers. The functional employees assigned to product teams change over time as the specific skills that the team needs change. At the beginning of the product

Figure 7.7
Matrix and
Product Team
Structures

A. MATRIX STRUCTURE



B. PRODUCT TEAM STRUCTURE



development process, for example, engineers and R&D specialists are assigned to a product team because their skills are needed to develop new products. When a provisional design has been established, marketing experts are assigned to the team to gauge how customers will respond to the new product. Manufacturing personnel join when it is time to find the most efficient way to produce the product. As their specific jobs are completed, team members leave and are reassigned to new teams. In this way the matrix structure makes the most use of human resources.

To keep the matrix structure flexible, product teams are empowered and team members are responsible for making most of the important decisions involved in product development.³⁵ The product team manager acts as a facilitator, controlling the financial resources and trying to keep the project on time and within budget.

The functional managers try to ensure that the product is the best that it can be in order to maximize its differentiated appeal.

High-tech companies that operate in environments where new product development takes place monthly or yearly have used matrix structures successfully for many years, and the need to innovate quickly is vital to the organization's survival. The flexibility afforded by a matrix structure allows managers to keep pace with a changing and increasingly complex environment.³⁶

PRODUCT TEAM STRUCTURE The dual reporting relationships that are at the heart of a matrix structure have always been difficult for managers and employees to deal with. Often, the functional boss and the product boss make conflicting demands on team members, who do not know which boss to satisfy first. Also, functional and product team bosses may come into conflict over precisely who is in charge of which team members and for how long. To avoid these problems, managers have devised a way of organizing people and resources that still allows an organization to be flexible but makes its structure easier to operate: a product team structure.

The **product team structure** differs from a matrix structure in two ways: (1) It does away with dual reporting relationships and two-boss employees, and (2) functional employees are permanently assigned to a cross-functional team that is empowered to bring a new or redesigned product to market. A **cross-functional team** is a group of managers brought together from different departments to perform organizational tasks. When managers are grouped into cross-departmental teams, the artificial boundaries between departments disappear, and a narrow focus on departmental goals is replaced with a general interest in working together to achieve organizational goals. The results of such changes have been dramatic: DaimlerChrysler can introduce a new model of car in two years, down from five; Black & Decker can innovate new products in months, not years; and Hallmark Cards can respond to changing customer demands for types of cards in weeks, not months.

Members of a cross-functional team report only to the product team manager or to one of his or her direct subordinates. The heads of the functions have only an informal, advisory relationship with members of the product teams—the role of functional managers is only to counsel and help team members, share knowledge among teams, and provide new technological developments that can help improve each team's performance (see Figure 7.7b).³⁷

Increasingly, organizations are making empowered cross-functional teams an essential part of their organizational architecture to help them gain a competitive advantage in fast-changing organizational environments. For example, Newell Rubbermaid, the well-known maker of more than 5,000 household products, moved to a product team structure because its managers wanted to speed up the rate of product innovation. Managers created 20 cross-functional teams composed of five to seven people from marketing, manufacturing, R&D, finance, and other functions.³⁸ Each team focuses its energies on a particular product line, such as garden products, bathroom products, or kitchen products. These teams develop more than 365 new products a year.

Hybrid structure

A large organization that has many divisions and simultaneously uses many different structures has a **hybrid structure**. Most large organizations use product

product team structure

An organizational structure in which employees are permanently assigned to a cross-functional team and report only to the product team manager or to one of his or her direct subordinates.

cross-functional team

A group of managers brought together from different departments to perform organizational tasks.

hybrid structure

The structure of a large organization that has many divisions and simultaneously uses many different organizational structures.

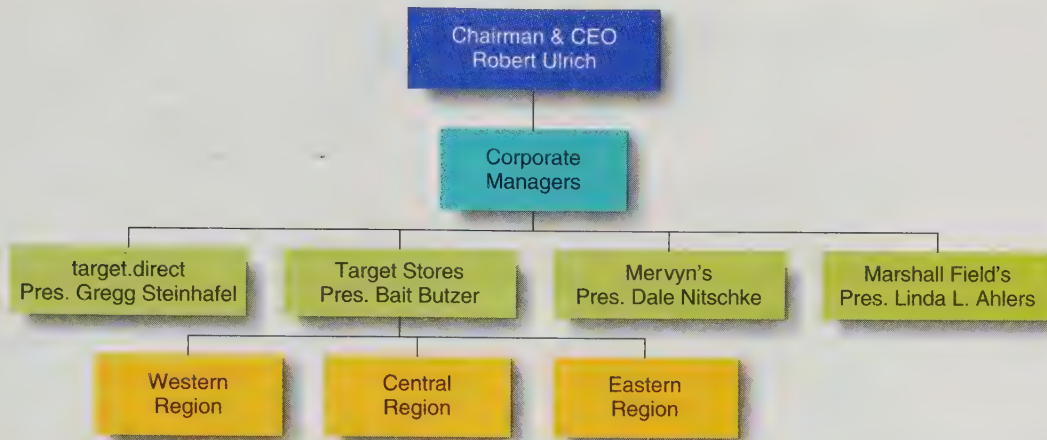


Figure 7.8
Target's Hybrid Structure

division structures and create self-contained divisions; then each division's managers select the structure that best meets the needs of the particular environment, strategy, and so on. Thus, one product division may choose to operate with a functional structure, a second may choose a geographic structure, and a third may choose a product team structure because of the nature of the division's products or the desire to be more responsive to customers' needs. Target uses a hybrid structure based on grouping by customer and by geography.

As shown in Figure 7.8, Target operates its different store chains as four independent divisions in a market division structure. Its four market divisions are Mervyn's and Marshall Field's, which cater to the needs of affluent customers; Target Stores, which competes in the low-price segment; and target.direct, Target's Internet division, which manages online sales.

Beneath this organizational layer is another layer of structure because both Target Stores and Marshall Field's operate with a geographic structure that groups stores by region. Individual stores are under the direction of a regional office, which is responsible for coordinating the market needs of the stores in its region and for responding to regional customer needs. The regional office feeds information back to divisional headquarters, where centralized merchandising functions make decisions for all Target or Marshall Field's stores.

Organizational structure may thus be likened to the layers of an onion. The outer layer provides the overarching organizational framework—most commonly a product or market division structure—and each inner layer is the structure that each division selects for itself in response to the contingencies it faces—such as a geographic or product team structure. The ability to break a large organization into smaller units or divisions makes it much easier for managers to change structure when the need arises—for example, when a change in technology or an increase in competition in the environment necessitates a change from a functional to a product team structure.

Coordinating Functions and Divisions

In organizing, managers have several tasks. The first is to group functions and divisions and create the organizational structures best suited to the contingencies they face. Their next task is to ensure that there is sufficient coordination or integration among functions and divisions so that organizational resources are used efficiently and effectively. Having

discussed how managers divide organizational activities into jobs, functions, and divisions to increase efficiency and effectiveness, we now look at how they put the parts back together.

We look first at the way in which managers design the hierarchy of authority to coordinate functions and divisions so that they work together effectively. Then we focus on integration and examine the many different integrating mechanisms that managers can use to coordinate functions and divisions.

Allocating authority

As organizations grow and produce a wider range of goods and services, the size and number of their functions and divisions increase. To coordinate the activities of people, functions, and divisions and to allow them to work together effectively, managers must develop a clear hierarchy of authority.⁴⁴ **Authority** is the power vested in a manager to make decisions and use resources to achieve organizational goals by virtue of his or her position in an organization. The **hierarchy of authority** is an organization's chain of command—the relative authority that each manager has—extending from the CEO at the top, down through the middle managers and first-line managers, to the nonmanagerial employees who actually make goods or provide services. Every manager, at every level of the hierarchy, supervises one or more subordinates. The term **span of control** refers to the number of subordinates who report directly to a manager.

Figure 7.9 (page 265) shows a simplified picture of the hierarchy of authority and the span of control of managers in McDonald's in 2004. At the top of the hierarchy is James Skinner, CEO and chairman of McDonald's board of directors, who took control in 2004.⁴⁵ Skinner is the manager who has ultimate responsibility for McDonald's performance, and he has the authority to decide how to use organizational resources to benefit McDonald's stakeholders.⁴⁶ Both Mike Roberts and Matthew Paull report directly to Skinner. Roberts is the CEO of McDonald's domestic operations; Paull is the Chief Financial Officer (CFO). They are next in the chain of command under Skinner. Of special mention is Ralph Alvarez, who in July 2004 was appointed as president of domestic operations, reporting to Roberts. Unlike the others, Paull is not a **line manager**, someone in the direct line or chain of command who has formal authority over people and resources. Rather, Paull is the **staff manager**, responsible for one of McDonald's specialist functions, finance.

Managers at each level of the hierarchy confer on managers at the next level down the authority to make decisions about how to use organizational resources. Accepting this authority, those lower-level managers then become responsible for their decisions and are accountable for how well they make those decisions. Managers who make the right decisions are typically promoted, and organizations motivate managers with the prospects of promotion and increased responsibility within the chain of command.

authority The power to hold people accountable for their actions and to make decisions concerning the use of organizational resources.

hierarchy of authority An organization's chain of command, specifying the relative authority of each manager.

span of control The number of subordinates who report directly to a manager.

line manager Someone in the direct line or chain of command who has formal authority over people and resources lower down.

staff manager A manager responsible for managing a specialist function, such as finance or marketing.

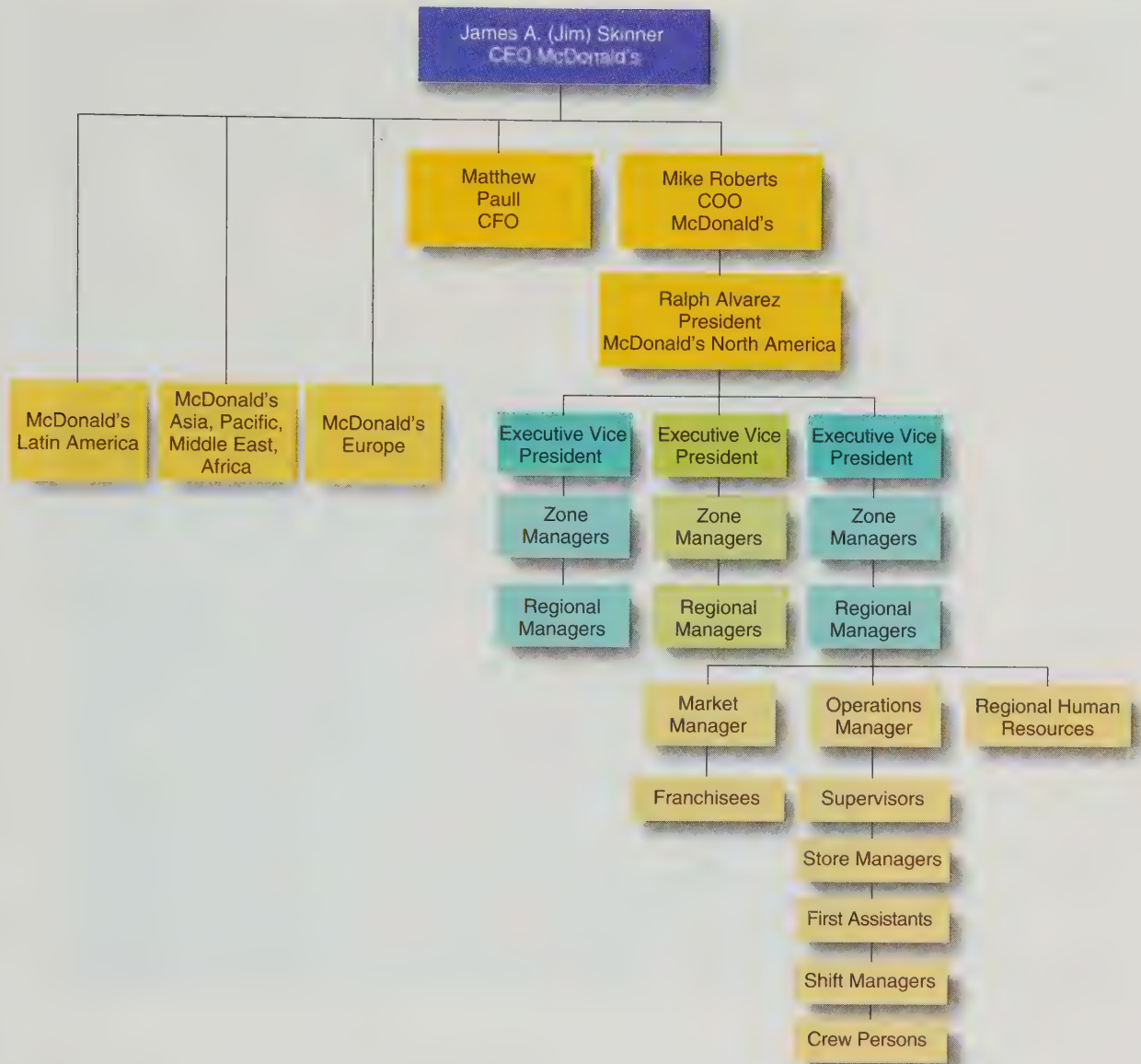


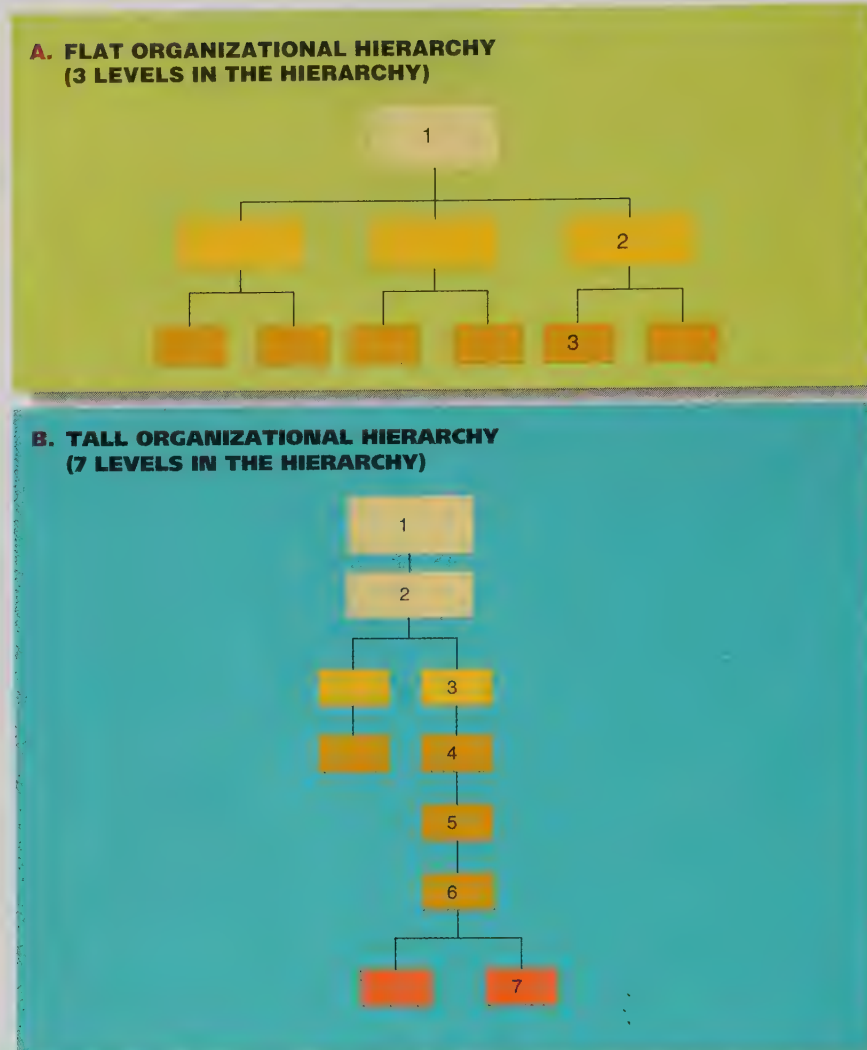
Figure 7.9

The Hierarchy of Authority and Span of Control at McDonald's Corporation

Below Roberts are the other main levels or layers in the McDonald's USA chain of command—executive vice presidents, zone managers, regional managers, and supervisors. A hierarchy is also evident in each company-owned McDonald's restaurant. At the top is the store manager; at lower levels are the first assistant, shift managers, and crew personnel. McDonald's managers have decided that this hierarchy of authority best allows the company to pursue its business-level strategy of providing fast food at reasonable prices.

TALL AND FLAT ORGANIZATIONS As an organization grows in size (normally measured by the number of its managers and employees), its hierarchy of

Figure 7.10
Tall and Flat
Organizations



authority normally lengthens, making the organizational structure taller. A *tall* organization has many levels of authority relative to company size; a *flat* organization has fewer levels relative to company size (see Figure 7.10, page 266).⁴⁷ As a hierarchy becomes taller, problems may result that make the organization's structure less flexible and slow managers' response to changes in the organizational environment.

Communication problems may arise when an organization has many levels in the hierarchy. It can take a long time for the decisions and orders of upper-level managers to reach managers further down in the hierarchy, and it can take a long time for top managers to learn how well their decisions worked. Feeling out of touch, top managers may want to verify that lower-level managers are following orders and may require written confirmation from them. Middle managers, who know they will be held strictly accountable for their actions, start devoting more time to the process of making decisions to improve their chances of being right. They might even try to avoid responsibility by making top managers decide what actions to take.

Another communication problem that can result is the distortion of commands and orders being transmitted up and down the hierarchy, which causes managers at different levels to interpret what is happening differently. Distortion of orders and messages can be accidental, occurring because different managers interpret messages from their own narrow, functional perspectives. Or distortion can be intentional, occurring because managers low in the hierarchy decide to interpret information in a way that increases their own personal advantage.

Another problem with tall hierarchies is that they usually indicate that an organization is employing many managers, and managers are expensive. Managerial salaries, benefits, offices, and secretaries are a huge expense for organizations. Large companies such as IBM and General Motors pay their managers billions of dollars a year. In the early 2000s, hundreds of thousands of middle managers were laid off as dot-coms collapsed and high-tech companies such as Hewlett-Packard and Lucent attempted to reduce costs by restructuring and downsizing their workforces.

THE MINIMUM CHAIN OF COMMAND To ward off the problems that result when an organization becomes too tall and employs too many managers, top managers need to ascertain whether they are employing the right number of middle and first-line managers and whether they can redesign their organizational architecture to reduce the number of managers. Top managers might well follow a basic organizing principle—the principle of the minimum chain of command—which states that top managers should always construct a hierarchy with the fewest levels of authority necessary to efficiently and effectively use organizational resources.

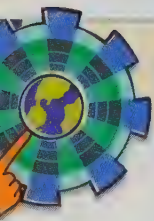
Effective managers constantly scrutinize their hierarchies to see whether the number of levels can be reduced—for example, by eliminating one level and giving the responsibilities of managers at that level to managers above and empowering employees below. This practice has become increasingly common in the United States as companies that are battling low-cost foreign competitors search for new ways to reduce costs. One manager who is constantly trying to empower employees and keep the hierarchy flat is Colleen C. Barrett, the number two executive of Southwest Airlines.⁴⁸ Barrett is the highest-ranking woman in the airline industry. At Southwest, she is well known for continually reaffirming Southwest's message that employees should feel free to go above and beyond their prescribed roles to provide better customer service. Her central message is that Southwest values and trusts its employees, who are empowered to take responsibility. Southwest employees are encouraged not to look to their superiors for guidance but, rather, to take responsibility to find ways to do the job better themselves. As a result, Southwest keeps the number of its middle managers to a minimum.

CENTRALIZATION AND DECENTRALIZATION OF AUTHORITY Another way in which managers can keep the organizational hierarchy flat is by decentralizing authority to lower-level managers and nonmanagerial employees.⁴⁹ If managers at higher levels give lower-level employees the responsibility of making important decisions and only manage by exception, then the problems of slow and distorted communication noted previously are kept to a minimum. Moreover, fewer managers are needed because their role is not to make decisions but to act as coach and facilitator and to help other employees make the best decisions. In addition, when decision making is low in the organization and near the customer, employees are better able to recognize and respond to customer needs.

Decentralizing authority allows an organization and its employees to behave in a flexible way even as the organization grows and becomes taller. This is why managers are so interested in empowering employees, creating self-managed work teams, establishing cross-functional teams, and even moving to a product team structure. These design innovations help keep the organizational architecture flexible and responsive to complex task and general environments, complex technologies, and complex strategies.

Although more and more organizations are taking steps to decentralize authority, too much decentralization has certain disadvantages. If divisions, functions, or teams are given too much decision-making authority, they may begin to pursue their own goals at the expense of organizational goals. Managers in engineering design or R&D, for example, may become so focused on making the best possible product that they fail to realize that the best product may be so expensive that few people will be willing or able to buy it. Also, with too much decentralization, lack of communication among functions or among divisions may prevent possible synergies among them from ever materializing, and organizational performance suffers.

Top managers must seek the balance between centralization and decentralization of authority that best meets the four major contingencies an organization faces (see Figure 7.1). If managers are in a stable environment, are using well-understood technology, and are producing staple kinds of products (such as cereal, canned soup, books, or televisions), then there is no pressing need to decentralize authority, and managers at the top can maintain control of much of organizational decision making.⁵⁰ However, in uncertain, changing environments where high-tech companies are producing state-of-the-art products, top managers must empower employees and allow teams to make important strategic decisions so that the organization can keep up with the changes taking place. Electronic circuit board maker Plexus, profiled in the following “Managing Globally,” provides a vivid example of the issues involved in decentralization.

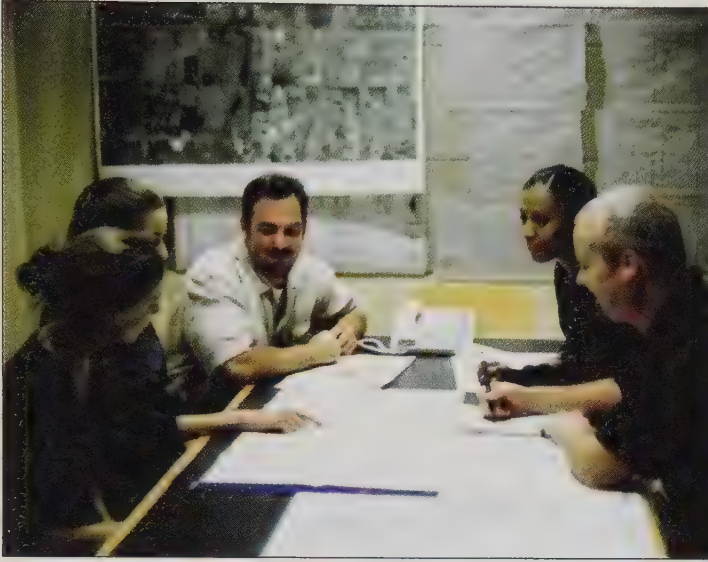


Managing Globally

Plexus Uses Self-Managed Teams to Decentralize Authority

In the United States, over 2.3 million manufacturing jobs were lost to factories in low-cost countries abroad in 2003. While many large U.S. manufacturing companies have given up the battle, some companies like electronics maker Plexus Corp., based in Neenah, Wisconsin, have been able to find a way of organizing that has allowed them to survive and prosper in a low-cost manufacturing world. How have they done this? By decentralizing control to empowered work teams.

In the 1990s, Plexus saw the writing on the wall as more and more of its customers began to turn to manufacturers abroad to produce the electronic components that go into their products or even the whole product itself. The problem facing managers at Plexus was how to organize work activities to compete in a low-cost manufacturing world. U.S. companies cannot match the efficiency of foreign manufacturers in producing high volumes of a *single* product, such as



Employees who are closest to customers are better able to recognize and respond to customer needs. As organizations become taller, managers realize the need to empower employees at all levels to make decisions that will positively influence customer relationships. This is why managers are so interested in creating self-managed work teams, cross-functional teams, and even moving to a product structure.

millions of a particular circuit board used in a laptop computer. So Plexus's managers decided to focus their efforts on developing a manufacturing technology called "low-high" that could efficiently produce low volumes of *many* different kinds of products.

Plexus's managers worked as a team to design an organizational structure based on creating four "focused factories" in which control over production decisions is given to the workers, who perform all the operations involved in making a product. To allow authority to be decentralized, Plexus's managers cross-trained workers so that they can perform any particular operation in their "factory." With this approach, when work slows down at any point in the production of a particular product, a worker further along the production process can move back to help solve the problem that has arisen at the earlier stage.⁵¹

Furthermore, managers organized workers into self-managed teams that are empowered to make all the decisions necessary to make a particular product in one of the four factories. Since each product is different, these teams have to quickly make the decisions necessary to assemble it if they are to do so in a cost-effective way—so decentralization is essential. The ability of these teams to make rapid decisions is vital on a production line, as time is money. Every minute a production line is not moving adds hundreds or thousands of dollars to production costs. So, to keep costs low, workers have to be able to decide how to react to unexpected contingencies and make nonprogrammed decisions. Another important reason for decentralization is that when a changeover takes place from making one product to making another, nothing is being produced and thus it is vital that changeover time be kept to a minimum. At Plexus, managers, by allowing teams to experiment and by providing guidance, have reduced changeover time to as little as 30 minutes. The line is running and making products 80 percent of the time; it is stopped for only 20 percent.⁵² This incredible flexibility, brought about by the way employees are organized, is the reason why Plexus is so efficient and can compete against low-cost manufacturers abroad.

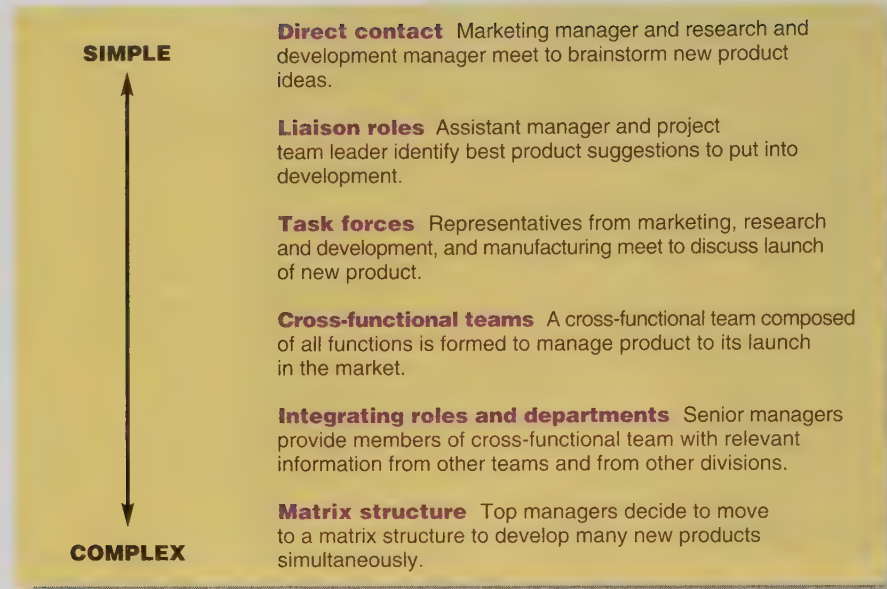
integrating mechanisms

Organizing tools that managers can use to increase communication and coordination among functions and divisions.

Types of integrating mechanisms

Much coordination takes place through the hierarchy of authority. In addition, managers can use various **integrating mechanisms** to increase communication and coordination among functions and divisions. The greater the complexity of an organization's structure, the greater is the need for coordination among people,

Figure 7.11
Types and
Examples of
Integrating
Mechanisms

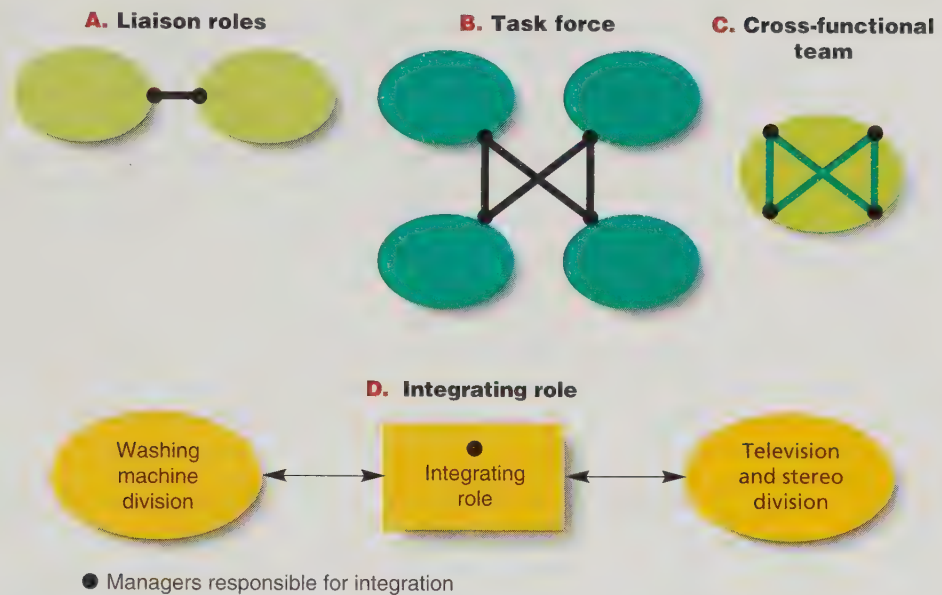


functions, and divisions to make the organizational structure work efficiently and effectively.⁵³ Thus, when managers choose to adopt a divisional, matrix, or product team structure, they must use complex kinds of integrating mechanisms to achieve organizational goals. UPS and FedEx, for example, have complex geographic structures that need an enormous amount of coordination among regions to achieve the goal of next-day package delivery. They achieve this through the innovative use of integrating mechanisms such as computer-controlled tracking equipment and customer-liaison personnel to manage transactions quickly and efficiently.

Six integrating mechanisms are available to managers to increase communication and coordination.⁵⁴ These mechanisms—arranged on a continuum from simplest to most complex—are listed in Figure 7.11 with examples of the individuals or groups that might use them. In the remainder of this section we examine each one, moving from the simplest to the most complex.

DIRECT CONTACT Direct contact among managers creates a context within which managers from different functions or divisions can work together to solve mutual problems. However, several problems are associated with establishing contact among managers in different functions or divisions. Managers from different functions may have different views about what must be done to achieve organizational goals. But if the managers have equal authority (as functional managers typically do), the only manager who can tell them what to do is the CEO. If functional and divisional managers cannot reach agreement, no mechanism exists to resolve the conflict apart from the authority of the boss. The need to solve everyday conflicts, however, wastes top-management time and effort and slows decision making. In fact, one sign of a poorly performing organizational structure is the number of problems sent up the hierarchy for top managers to solve. To increase coordination among functions and divisions and to prevent these problems from emerging, top managers can incorporate more complex integrating mechanisms into their organizational architecture.

Figure 7.12
Forms of
Integrating
Mechanisms



LIAISON ROLES Managers can increase coordination among functions and divisions by establishing liaison roles. When the volume of contacts between two functions increases, one way to improve coordination is to give one manager in each function or division the responsibility for coordinating with the other. These managers may meet daily, weekly, monthly, or as needed. Figure 7.12a depicts a liaison role; the small dot represents the person within a function who has responsibility for coordinating with the other function. The responsibility for coordination is part of the liaison's full-time job, and usually an informal relationship forms between the people involved, greatly easing strains between functions. Furthermore, liaison roles provide a way of transmitting information across an organization, which is important in large organizations whose employees may know no one outside their immediate function or division.

TASK FORCES When more than two functions or divisions share many common problems, direct contact and liaison roles may not provide sufficient coordination. In these cases, a more complex integrating mechanism, a **task force**, may be appropriate (see Figure 7.12b). One manager from each relevant function or division is assigned to a task force that meets to solve a specific, mutual problem; members are responsible for reporting back to their departments on the issues addressed and the solutions recommended. Task forces are often called *ad hoc* committees because they are temporary; they may meet on a regular basis or only a few times. When the problem or issue is solved, the task force is no longer needed; members return to their normal roles in their departments or are assigned to other task forces. Typically, task force members also perform many of their normal duties while serving on the task force.

CROSS-FUNCTIONAL TEAMS In many cases, the issues addressed by a task force are recurring problems, such as the need to develop new products or find new kinds of customers. To address recurring problems effectively, managers are increasingly using permanent integrating mechanisms such as cross-functional teams

task force A committee of managers from various functions or divisions who meet to solve a specific, mutual problem; also called *ad hoc* committee.

(see Figure 7.12c). An example of a cross-functional team is a new product development committee that is responsible for the choice, design, manufacturing, and marketing of a new product. Such an activity obviously requires a great deal of integration among functions if new products are to be successfully introduced, and using a complex integrating mechanism such as a cross-functional team accomplishes this. Intel, for instance, emphasizes cross-functional teamwork. Its structure consists of over 90 cross-functional groups that meet regularly to set functional strategy in areas such as engineering and marketing and to develop business-level strategy.

The more complex an organization, the more important cross-functional teams become. Westinghouse, for example, has established a cross-functional team system to promote integration among divisions and improve organizational performance. As discussed previously, the product team structure is based on cross-functional teams to speed products to market. These teams assume responsibility for all aspects of product development.

INTEGRATING ROLES An *integrating role* is a role whose only function is to increase coordination and integration among functions or divisions to achieve performance gains from synergies (see Figure 7.12d). Usually, managers who perform integrating roles are experienced senior managers who can envisage how to use the resources of the functions or divisions to obtain new synergies. One study found that Du Pont, the giant chemical company, had created 160 integrating roles to provide coordination among the different divisions of the company and improve corporate performance.⁵⁵ Once again, the more complex an organization and the greater the number of its divisions, the more important integrating roles are.

MATRIX STRUCTURE When managers must be able to respond quickly to the task and general environments, they often use a matrix structure. The reason for choosing a matrix structure is clear. It contains many of the integrating mechanisms already discussed: The two-boss employees integrate between functions and product teams; the matrix is built on the basis of temporary teams or task forces; and each member of a team performs a liaison role. The matrix structure is flexible precisely because it is formed from complex integrating mechanisms.

In summary, to keep an organization responsive to changes in its task and general environments as the organization grows and becomes more complex, managers must increase coordination among functions and divisions by using complex integrating mechanisms. Managers must decide on the best way to organize their structures to create an organizational architecture that allows them to make the best use of organizational resources.

strategic alliance

An agreement in which managers pool or share their organization's resources and know-how with a foreign company and the two organizations share the rewards and risks of starting a new venture.

Strategic Alliances, B2B Network Structures, and IT

Recently, increasing globalization and the use of new IT have brought about two innovations in organizational architecture that are sweeping through U.S. and European companies: strategic alliances and business-to-business (B2B) network structures. A **strategic alliance** is a formal agreement that commits two or more companies to exchange or share their resources in order to produce and market a product.⁵⁶ Most commonly strategic alliances are formed because the companies share similar interests and believe they can benefit from cooperating. For example, Japanese car companies such as Toyota and Honda

have formed many strategic alliances with particular suppliers of inputs such as car axles, gearboxes, and air-conditioning systems. Over time, these car companies work closely with their suppliers to improve the efficiency and effectiveness of the inputs so that the final product—the car produced—is of higher quality and very often can be produced at lower cost. Toyota and Honda have also established alliances with suppliers throughout the United States and Mexico because both companies now build several models of cars in these countries.

Throughout the 1990s, the growing sophistication of IT with global intranets and teleconferencing has made it much easier to manage strategic alliances and allow managers to share information and cooperate. One outcome of this has been the growth of strategic alliances into a network structure. A **network structure** is a series of global strategic alliances that one or several organizations create with suppliers, manufacturers, and/or distributors to produce and market a product. Network structures allow an organization to manage its global value chain in order to find new ways to reduce costs and increase the quality of products—without incurring the high costs of operating a complex organizational structure (such as the costs of employing many managers). More and more U.S. and European companies are relying on global network structures to gain access to low-cost foreign sources of inputs, as discussed in Chapter 6. Shoemakers such as Nike and Adidas are two companies that have used this approach extensively.

Nike is the largest and most profitable sports shoe manufacturer in the world. The key to Nike's success is the network structure that Nike founder and CEO Philip Knight created to allow his company to produce and market shoes. As noted in Chapter 6, the most successful companies today are trying to pursue simultaneously a low-cost and a differentiation strategy. Knight decided early that to do this at Nike he needed organizational architecture that would allow his company to focus on some functions, such as design, and leave others, such as manufacturing, to other organizations.

By far the largest function at Nike's Oregon headquarters is the design function, composed of talented designers who pioneered innovations in sports shoe design such as the air pump and Air Jordans that Nike introduced so successfully. Designers use computer-aided design (CAD) to design Nike shoes, and they electronically store all new product information, including manufacturing instructions. When the designers have finished their work, they electronically transmit all the blueprints for the new products to a network of Southeast Asian suppliers and manufacturers with which Nike has formed strategic alliances.⁵⁷ Instructions for the design of a new sole may be sent to a supplier in Taiwan; instructions for the leather uppers, to a supplier in Malaysia. The suppliers produce the shoe parts and send them for final assembly to a manufacturer in China with which Nike has established another strategic alliance. From China the shoes are shipped to distributors throughout the world. Ninety-nine percent of the 99 million pairs of shoes that Nike makes each year are made in Southeast Asia.

This network structure gives Nike two important advantages. First, Nike is able to respond to changes in sports shoe fashion very quickly. Using its global IT system, Nike literally can change the instructions it gives each of its suppliers overnight, so that within a few weeks its foreign manufacturers are producing new kinds of shoes.⁵⁸ Any alliance partners that fail to perform up to Nike's standards are replaced with new partners.

Second, Nike's costs are very low because wages in Southeast Asia are a fraction of what they are in the United States, and this difference gives Nike a low-cost

network structure

A series of strategic alliances that an organization creates with suppliers, manufacturers, and/or distributors to produce and market a product.

outsource To use outside suppliers and manufacturers to produce goods and services.

advantage. Also, Nike's ability to **outsource** and use foreign manufacturers to produce all its shoes abroad allows Knight to keep the organization's U.S. structure flat and flexible. Nike is able to use a relatively inexpensive functional structure to organize its activities. However, sports shoe manufacturers' attempts to keep their costs low have led to many charges that Nike and others are supporting sweatshops that harm foreign workers, as the following "Ethics in Action" suggests.

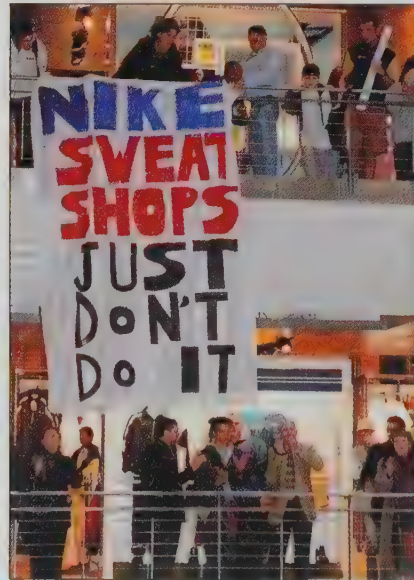


Ethics in Action

Of Shoes and Sweatshops

As the production of all kinds of goods and services is being increasingly outsourced to poor regions and countries of the world, the behavior of companies that outsource production to subcontractors in these countries has come under increasing scrutiny. Nike, the giant sports shoe maker with sales of more than \$9 billion a year, was one of the first to experience a backlash when critics revealed how workers in these countries were being treated. Indonesian workers were stitching together shoes in hot, noisy factories for only 80 cents a day or about \$18 a month.⁵⁹ Workers in Vietnam and China fared better; they could earn \$1.60 a day. In all cases, however, critics charged that at least \$3 a day was needed to maintain an adequate living standard.

These facts generated an outcry in the United States, where Nike was roundly attacked for its labor practices; a backlash against sales of Nike products forced Phil Knight, Nike's billionaire owner, to reevaluate Nike's labor practices. Nike announced that henceforth all the factories producing its shoes and clothes would be independently monitored and inspected. After its competitor Reebok, which also had been criticized for similar labor practices, announced that it was raising wages in Indonesia by 20 percent, Nike raised them by 25 percent to \$23 a month.⁶⁰ Small though this may seem, it was a huge increase to workers in these countries.



Members of United Students against Nike unfurl a banner at the Niketown store in New York accusing Nike of using sweatshop labor to produce its athletic apparel. Nike and other athletic apparel companies have since taken steps to ensure better working conditions for foreign workers.

In Europe, another sportswear company, Adidas, had largely escaped such criticism. But in 1999 it was reported that in El Salvador, a Taiwan-based Adidas subcontractor was employing girls as young as 14 in its factories and making them work for more than 70 hours a week. They were allowed to go to the restroom only twice a day, and if they stayed longer than three minutes, they lost a day's wages.⁶¹ Adidas moved swiftly to avoid the public relations nightmare that Nike had experienced. Adidas announced that henceforth its subcontractors would be required to abide by more strict labor standards.

What happened in the sports shoe industry has happened throughout the clothing industry as well as other industries like electronics and toys in the 2000s. Companies such as Wal-Mart, Target, The Gap, Sony, and Mattel have all been forced to reevaluate the ethics of their labor practices and to promise to keep a constant watch on subcontractors in the future. A statement to this effect can be found on many of these companies' Web pages, for example, Nike's (www.nikebiz.com) and The Gap's (www.thegap.com), as mentioned in Chapter 3.

The ability of managers to develop a network structure to produce or provide the goods and services customers want, rather than create a complex organizational structure to do so, has led many researchers and consultants to popularize the idea of a **boundaryless organization**. Such an organization is composed of people linked by IT—computers, faxes, computer-aided design systems, and video teleconferencing—who may rarely, if ever, see one another face-to-face. People are utilized when their services are needed, much as in a matrix structure, but they are not formal members of an organization; they are functional experts who form an alliance with an organization, fulfill their contractual obligations, and then move on to the next project.

Large consulting companies, such as Arthur Andersen and McKinsey & Co., utilize their global consultants in this way. Consultants are connected by laptops to an organization's **knowledge management system**, its company-specific information system that systematizes the knowledge of its employees and provides them with access to other employees who have the expertise to solve the problems that they encounter as they perform their jobs.

The use of outsourcing and the development of network structures is increasing rapidly as organizations recognize the many opportunities they offer to reduce costs and increase organizational flexibility. U.S. companies spent \$300 billion on global supply chain management in 2000. This push to lower costs has led to the development of electronic **business-to-business (B2B) networks** in which most or all of the companies in an industry (for example, carmakers) use the same software platform to link to each other and establish industry specifications and standards. Then, these companies jointly list the quantity and specifications of the inputs they require and invite bids from the thousands of potential suppliers around the world. Suppliers also use the same software platform, so electronic bidding, auctions, and transactions are possible between buyers and sellers around the world. The idea is that high-volume standardized transactions can help drive down costs at the industry level.

Today, with advances in IT, designing organizational architecture is becoming an increasingly complex management function. To maximize efficiency and effectiveness, managers must assess carefully the relative benefits of having their own organization perform a functional activity versus forming an alliance with another organization to perform the activity. It is still not clear how B2B networks and other forms of electronic alliances between companies will develop in the future.

boundaryless

organization An organization whose members are linked by computers, faxes, computer-aided design systems, and video teleconferencing and who rarely, if ever, see one another face-to-face.

knowledge management system

A company-specific virtual information system that allows workers to share their knowledge and expertise and find others to help solve ongoing problems.

business to business (B2B) network

A group of organizations that join together and use IT to link themselves to potential global suppliers to increase efficiency and effectiveness.

Summary and Review

DESIGNING ORGANIZATIONAL STRUCTURE

The four main determinants of organizational structure are the external environment, strategy, technology, and human resources. In general, the higher the level of uncertainty associated with these factors, the more appropriate is a flexible, adaptable structure as opposed to a formal, rigid one.

GROUPING TASKS INTO JOBS Job design is the process by which managers group tasks into jobs. To create more interesting jobs, and to get workers to act flexibly, managers can enlarge and enrich jobs. The job characteristics model provides a tool managers can use to measure how motivating or satisfying a particular job is.

GROUPING JOBS INTO FUNCTIONS AND DIVISIONS Managers can choose from many kinds of organizational structures to make the best use of organizational resources. Depending on the specific organizing problems they face, managers can choose from functional, product, geographic, market, matrix, product team, and hybrid structures.

COORDINATING FUNCTIONS AND DIVISIONS No matter which structure managers choose, they must decide how to distribute authority in the organization, how many levels to have in the hierarchy of authority, and what balance to strike between centralization and decentralization to keep the number of levels in the hierarchy to a minimum. As organizations grow, managers must increase integration and coordination among functions and divisions. Six integrating mechanisms are available to facilitate this: direct contact, liaison roles, task forces, cross-functional teams, integrating roles, and the matrix structure.

STRATEGIC ALLIANCES, B2B NETWORK STRUCTURES, AND IT To avoid many of the communication and coordination problems that emerge as organizations grow, managers are attempting to use IT to develop new ways of organizing. In a strategic alliance, managers enter into an agreement with another organization to provide inputs or to perform a functional activity. If managers enter into a series of these agreements, they create a network structure. A network structure, most commonly based on some shared form of IT, can be formed around one company, or a number of companies can join together to create an industry B2B network.



Management in Action

Topics for Discussion and Action

Discussion

1. Would a flexible or a more formal structure be appropriate for these organizations: (a) a large department store, (b) a Big Five accountancy firm, (c) a biotechnology company? Explain your reasoning.
2. Using the job characteristics model as a guide, discuss how a manager can enrich or enlarge subordinates' jobs.
3. How might a salesperson's job or a secretary's job be enlarged or enriched to make it more motivating?

4. When and under what conditions might managers change from a functional to (a) a product, (b) a geographic, or (c) a market structure?
5. How do matrix structure and product team structure differ? Why is product team structure more widely used?

Action

6. Compare the pros and cons of using a network structure to perform organizational activities and performing all activities in-house or within one organizational hierarchy.
7. What are the advantages and disadvantages of business-to-business networks?

8. Find a manager and identify the kind of organizational structure that his or her organization uses to coordinate its people and resources. Why is the organization using that structure? Do you think a different structure would be more appropriate? Which one?
9. With the same or another manager, discuss the distribution of authority in the organization. Does the manager think that decentralizing authority and empowering employees is appropriate?



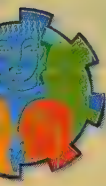
Building Management Skills

Understanding Organizing

Think of an organization with which you are familiar, perhaps one you have worked in—such as a store, restaurant, office, church, or school. Then answer the following questions:

1. Which contingencies are most important in explaining how the organization is organized? Do you think it is organized in the best way?
2. Using the job characteristics model, how motivating do you think the job of a typical employee in this organization is?
3. Can you think of any ways in which a typical job could be enlarged or enriched?
4. What kind of organizational structure does the organization use? If it is part of a chain, what kind of structure does the entire organization use? What other structures discussed in the chapter might allow the organization to operate more effectively? For example, would the move to a product team structure lead to greater efficiency or effectiveness? Why or why not?
5. How many levels are there in the organization's hierarchy? Is authority centralized or decentralized? Describe the span of control of the top manager and of middle or first-line managers.
6. Is the distribution of authority appropriate for the organization and its activities? Would it be possible to flatten the hierarchy by decentralizing authority and empowering employees?
7. What are the principal integrating mechanisms used in the organization? Do they provide sufficient coordination among individuals and functions? How might they be improved?
8. Now that you have analyzed the way this organization is organized, what advice would you give its managers to help them improve the way it operates?





Small Group Breakout Exercise

Bob's Appliances

Form groups of three or four people, and appoint one member as the spokesperson who will communicate your findings to the whole class when called on by the instructor. Then discuss the following scenario.

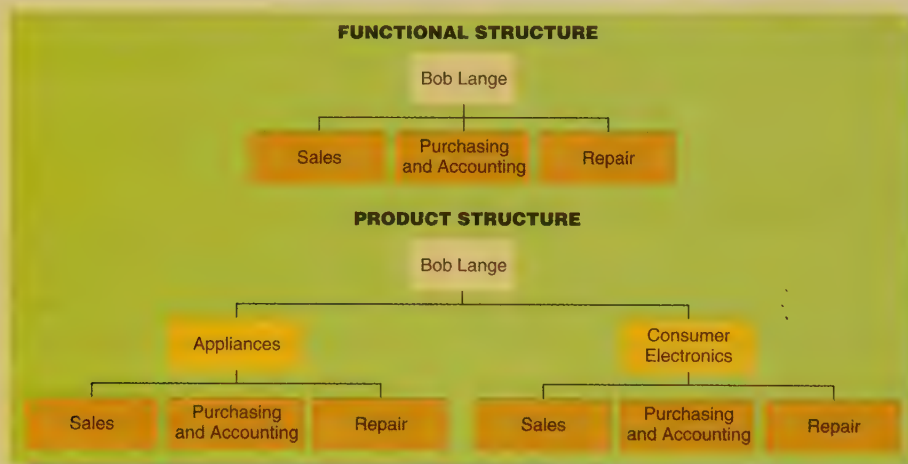
Bob's Appliances sells and services household appliances such as washing machines, dishwashers, ranges, and refrigerators. Over the years, the company has developed a good reputation for the quality of its customer service, and many local builders patronize the store. Recently, some new appliance retailers, including Circuit City and REX, have opened stores that also provide numerous appliances. In addition to appliances, however, to attract more customers these stores carry a complete range of consumer electronics products—

televisions, stereos, and computers. Bob Lange, the owner of Bob's Appliances, has decided that if he is to stay in business, he must widen his product range and compete directly with the chains.

In 2002, he decided to build a 20,000-square-foot store and service center, and he is now hiring new employees to sell and service the new line of consumer electronics. Because of his company's increased size, Lange is not sure of the best way to organize the employees. Currently, he uses a functional structure; employees

are divided into sales, purchasing and accounting, and repair. Bob is wondering whether selling and servicing consumer electronics is so different from selling and servicing appliances that he should move to a product structure (see figure) and create separate sets of functions for each of his two lines of business.⁶²

You are a team of local consultants whom Bob has called in to advise him as he makes this crucial choice. Which structure do you recommend? Why?



Be the Manager

Speeding Up Web-Site Design

You have been hired by a Web-site design, production, and hosting company whose new animated Web-site designs are attracting a lot of attention and a lot of customers. Currently, employees are organized into different functions such as hardware, software design,

graphic art, and Web-site hosting, as well as functions such as marketing and human resources. Each function takes its turn to work on a new project from initial customer request to final online Web-site hosting.

The problem the company is experiencing is that it typically takes one year from the initial idea stage to the time that the Web site is up and running; the company wants to

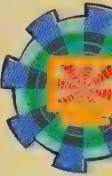
shorten this time by half to protect and expand its market niche. In talking to other managers, you discover that they believe the company's current functional structure is the source of the problem—it is not allowing employees to develop Web sites fast enough to satisfy customers' demands. They want you to design a better one.

Questions

1. Discuss ways in which you can improve the way the current functional structure operates so that it speeds Web-site development.
2. Discuss the pros and cons of moving to a (a) multidivisional, (b) matrix, and (c) product team structure to reduce Web-site development time.
3. Which of these structures do you think is most appropriate and why?

Additional Activities on the Build Your Management Skills DVD

- **Test Your Knowledge:**
 - (1) Mechanistic versus Organic Organizational Structures and
 - (2) Allocating Authority
- **Self Assessment:** Identify Your Preferred Organizational Structure
- **Manager's Hot Seat:** Virtual Workplace: Out of Office Reply



Managing Ethically

Suppose an organization is downsizing and laying off many of its middle managers. Some top managers charged with deciding who to terminate might decide to keep the subordinates they like, and who are obedient to them, rather than the ones who are difficult or the best performers. They might also decide to lay off the most highly paid subordinates even if they are high performers. Think of the ethical issues involved in de-

signing a hierarchy, and discuss the following issues.

Questions

1. What ethical rules (see Chapter 4) should managers use to decide which employees to terminate when redesigning their hierarchy?
2. Some people argue that employees who have worked for an organization for many

years have a claim on the organization at least as strong as that of its shareholders. What do you think of the ethics of this position—can employees claim to “own” their jobs if they have contributed significantly to its past success? How does a socially responsible organization behave in this situation?



BusinessWeek

Case in the News

No Excuse Not to Succeed

Dressed in a cream-colored suit amid a sea of dark jackets, Antonio M. Perez looked more like an MC of a glitzy Vegas show than a corporate chieftain as he took the stage before a standing-room-only crowd of camera-shop owners and photo buffs in America's gambling mecca. And the chief operating officer of Eastman Kodak Co. displayed a showman's bravado when he declared: “Kodak holds a winning hand.”

Certainly, some in the room figured Perez was bluffing. Kodak is desperately trying to reinvent itself for the Digital Age, and 58-year-old

Perez, who oversaw Hewlett-Packard Co.'s rise to dominance in inkjet printers, was hired a year ago to lead the way. Kodak is in a race against time as its traditional film business disappears; Sales peaked at \$14 billion in 1999 and have dropped to \$13.3 billion in 2003. Today, Kodak finds itself in the awkward position of having to establish itself in a field dominated by others.

It's a painful irony for the company. For a century, Kodak enjoyed near-monopoly power—until Fuji Photo Film Co. came along. Kodak even came up with the first digital camera in 1975. But it is only now that the company is starting to capitalize on the technology.

Clear Vision

Perez has gotten off to a quick start at a company once known for its destructively slow decision-making. He has made clear what many at the Rochester (N.Y.) headquarters long denied—that Kodak's main business has to be digital imaging. In September, the company announced a sharper focus on digital businesses for its consumer, commercial, and health units that it predicts will increase the company's revenue 23 percent, to \$16 billion, in 2006, and to \$20 billion by 2010.

Perez helped figure out how to pay for the transition—mostly by reducing investment in film and laying off nearly a quarter of Kodak's

60,000 workforce. He has instilled a new discipline at the company that is speeding product development. And he is uncovering new uses for Kodak's 20,000 patents. "The intellectual property and know-how is unbelievable in the company," he says. "There is no excuse not to succeed."

But the toughest challenges still lie ahead. Perez has to get Kodak's engineers and marketers to work together to come up with products that will hold their own in areas where the company has little credibility. For example, after rummaging around Kodak's hallowed labs, Perez believes he has found a breakthrough technology that will change the inkjet printer business. And that is all he will say.

Sounds like wishful thinking to some. "It's not about patents. It's all about commercializing the technology," says Vyomesh Joshi, who worked under Perez at HP and now runs its imaging and printing group. "That's where they're going to have a hard time."

Perez, for all his showy enthusiasm, is well aware of the old attitude problems at Big Yellow. The biggest is a strange complacency—some call it arrogance—when it comes to

selling what are widely acknowledged to be innovative products. "They tend to bring out one product and think, that's it—that they've now solved all the problems and the world will beat a path to their door," says Frank J. Romano, a professor of printing at Rochester Institute of Technology. The printer dock for the Kodak EasyShare digital camera is a case in point. Introduced last year, the dock finally made it easy for digital shutterbugs to print their photos without a computer. If, that is, they used a Kodak camera. Such proprietary standards are a no-no in the digital world. Although the dock topped \$100 million in sales in its first year, it could have done much better. Now Kodak is looking for ways to make the dock work with other cameras.

Perez has helped change how Kodak operates to ensure the company doesn't make the same mistake again. He has sharpened the focus of an integrated product-delivery program that helps marketers and gearheads work more closely together. And Perez has sped the reorganization of each Kodak business unit into special product groups. These are teams dedicated to specific areas such as

digital cameras, online services, or photo kiosks. By partly tying compensation to each group's performance, he expects better results.

Some employees and customers already note a faster pace. Kodak introduced six new digital cameras in February, double last year's number. And it raced to upgrade 3,300 photo-processing kiosks at CVS drugstores to wirelessly handle photos from camera phones. The old Kodak might have discouraged the change because it could cut into sales of disposable cameras.

Perez has found a company that for all its earlier conceit now sees the need for a change. That gives him a chance to turn Kodak into something it hasn't been for a while: a company whose best years are ahead of it.

Questions

1. What kinds of problems has Kodak been experiencing?
2. How has Kodak's COO been changing its organizational structure and design to respond to these problems?

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How Xerox Got Up to Speed

Xerox Corp. thought it was doing a smart thing when it consolidated 36 administrative centers into 3 back in 1999. The copy king would be able to reap millions in cost savings. But the move came just as Xerox was also reorganizing its sales division. The simultaneous upheaval in two key units unleashed chaos across the com-

pany's billing system. Customers received invoices quoting prices they had never agreed to—or detailing equipment they had never ordered. Worse, the mistakes took months to sort out, prompting some longtime customers to defect. The so-called document company had failed miserably at its own documentation.

Five years later, Xerox can see the bright side of that fiasco. After struggling to fix the problem itself, it

hired General Electric Capital to handle its billing. GE brought more than order to the process: It showed Xerox a whole new way to diagnose and fix its problems. If the company could omit steps from its design, manufacturing, and servicing processes, as well as fine-tune those that remained, it would be able to deliver better printers and copiers to customers far faster and at lower cost. "GE made progress with [our operations] much more

quickly than we could,” says Ursula M. Burns, president of Xerox Business Group Operations. Today, GE continues to handle Xerox’s billing.

What did GE have that Xerox didn’t? For one, years of experience in applying Six Sigma, the data-driven technique for eliminating defects in any business process. But GE had moved beyond Six Sigma to apply so-called lean manufacturing tools made famous by Toyota Motor Corp. in the 1980s. The combination—known as Lean Six Sigma—has taken root across corporate America in the past two years. Companies are using the techniques to analyze and improve tasks ranging from simple processes such as customer credit checks to complex product-design challenges. “Companies are starting to realize this is becoming a very competitive weapon,” says Deborah Nightingale, engineering systems director of Massachusetts Institute of Technology’s lean aerospace initiative.

Xerox kicked into high gear in late 2002 with training for top execs, including CEO Anne M. Mulcahy, who has spearheaded the effort. The company has since launched about 250 projects, both for itself and its customers. “We’ve gone at it with a vengeance,” says Mulcahy. And the results are already rolling in: Xerox claims a \$6 million return in 2003 on a \$14 million investment in Lean Six Sigma. It expects an even bigger payoff this year.

One of the strengths of Lean Six Sigma is that it blankets the company. Previous quality initiatives may have addressed a particular factory operation or only a part of it. The point is not to automate complicated processes, but to “lean out” existing processes by removing unnecessary steps and then fix those that remain.

Sounds easy, but Mulcahy admits it can be a slog. Learning the dozens of analytical methods involved in Lean Six Sigma takes weeks of training. Figuring out what steps to trim or replace chews up time, too. But the hardest task is getting employees to accept that how they’ve always done things may not be the best way. “A lot of the work is soft, not hard,” says Burns. But consultants say Xerox is succeeding because the CEO has made the program a priority. The head of the effort reports directly to Mulcahy, who herself is training to reach the yellow-belt level in the karate-like Lean Six Sigma regimen.

One of the “soft” challenges is tearing down walls to get different divisions to work together. This is never easy in a complex, big organization. Yet at Xerox, teams from supply, manufacturing, and research and development pulled it off to resolve a problem with a \$500,000 printing press introduced last year. Customers quickly found that the fuser roll (which uses heat and pressure to bond toner to paper) was wearing out sooner than expected. The Xerox team used Lean Six Sigma tools to zero in on the cause in just one month. The oil on the roller was fouling up the works. “Not only had the chemical structure of the oil changed, but we didn’t have enough of the oil that did work well,” says John R. Laing, senior vice president for Xerox’ supplies-delivery unit. The team worked with the oilmaker, which changed the chemistry, saving Xerox \$2 million and keeping its customers happy.

Ultimately, Xerox’s efforts are focused on getting new products to customers faster, which has meant taking steps out of the design process. Typically a high-end, \$200,000 machine that can print

100 pages a minute takes three to five cycles of design, building, and testing before it reaches the customer. Taking just one of those cycles out of the process can shave up to a year off the time to market. For its new DocuTech print-on-demand machines launched in January, for example, Xerox used software to simulate an early design stage, saving the time and expense of building a prototype.

These days, Xerox has gotten so good at applying Lean Six Sigma that, like GE before, it’s helping out its customers. In one case, the mail volume at a customer’s document-management unit had grown out of control. Xerox moved in, streamlined the mailroom—with changes as simple as removing furniture—to use half the amount of space, and saved the company \$180,000 in the process. From failing to fix its own operations to improving those of others is a big leap. Says Laing: “We’ve moved from being consciously incompetent to consciously competent.” Now, Mulcahy is pushing Xerox to become unconsciously competent—the point where the tools are so ingrained that no one even thinks about them anymore.

Questions

1. What problems arose when Xerox first changed its organizational structure? Why did these problems arise?
2. How has the company been using six Sigma to solve its problems? How have these changes affected Xerox’s organizational structure?

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CHAPTER

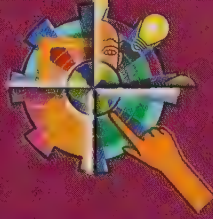
8

Control, Change, and Entrepreneurship

Learning Objectives

After studying this chapter, you should be able to:

- Define organizational control, and describe the four steps of the control process.
- Identify the main output controls, and discuss their advantages and disadvantages as means of coordinating and motivating employees.
- Identify the main behavior controls, and discuss their advantages and disadvantages as means of coordinating and motivating employees.
- Explain the role of clan control or organizational culture in creating an effective organizational architecture.
- Discuss the relationship between organizational control and change, and explain why managing change is a vital management task.
- Understand the role of entrepreneurship in the control and change process.



Management Snapshot

Control Is No Longer a Problem for Oracle

How should managers use control to improve performance?

Oracle is the second largest independent software company after Microsoft. Like Bill Gates, Microsoft's chairman, Oracle's co-founder and chairman, Larry Ellison, recognized that his company had a major problem in the early 2000s: Oracle was not using the latest Internet software—software developed by Oracle to control its activities—even though Oracle's customers were! As a result, Oracle was having a difficult time understanding its customers' needs, and internally the company was not experiencing the cost savings that result from implementing its own database and financial control software. Ellison moved quickly to change Oracle's control systems so that they were Internet based.

One of the main advantages of Internet-based control software is that it permits the centralized management of a company's widespread operations. Corporate managers can easily compare and contrast the performance of different divisions spread throughout the globe in real time and can quickly identify

problems and take corrective action. However, to his embarrassment, Ellison discovered that Oracle's financial and human resource information was located on over 70 different computing systems across the world. Tracking basic information such as the size of the com-



Employees discuss a project at Oracle headquarters in Redwood City, CA. Ironically, Oracle Chairman Larry Ellison realized the company had a major problem because it wasn't using the latest Internet-based control software—software it had developed itself!

pany's workforce and the sales of its leading products took time and effort. As a result, corrective action took a long time to complete and many opportunities were being missed.

Recognizing the irony of the situation, Ellison ordered his managers to change the way the company controlled—that is,

monitored and evaluated—its activities and to implement its new Internet-based control systems as quickly as possible. His goal was to have all of Oracle's sales, cost, profit, and human resource information systems consolidated in two locations and to make this information immediately available to managers throughout the company with one click of a mouse. In addition, Ellison instructed managers to investigate the kinds of activities monitored and controlled by people and wherever possible to substitute Internet-based control. For example, previously Oracle had over 300 people responsible for monitoring and managing such tasks as paper-based travel planning and expense report systems. These tasks were automated into software systems and put online, and employees were made responsible for filing their own reports. These same 300 people then were transferred into sales and consulting positions. The savings was over \$1 billion a year.¹

By using Internet software-based control systems, Oracle's managers also are able to get closer to their customers. All Oracle

salespeople received new customer relationship management software with instructions to enter detailed information into the system regarding customers' purchases, future plans, Web orders, and service requests. As a result, headquarters managers can track sales orders easily, and if the managers see problems such as lost sales or multiple service requests, they can contact customers quickly to solve problems and so build better customer relations.

So amazed has Ellison been at the result of implementing Internet software systems that he has radically rethought Oracle's control systems. He now believes that because of the advances of modern computer information systems, Oracle's employees should be doing only one of three things: building its products, servicing its products, or selling its products and the manager's job should be to use control only to facilitate one of these three front-line activities. All other activities should be automated by developing new information control systems.

Overview

As the experience of Oracle suggests, the ways in which managers decide to control the behavior of their employees can have very different effects on the way employees behave. When managers make choices about how to influence and regulate their employees' behavior and performance, they establish the second foundation of organizational architecture, organizational control. And control is the essential ingredient that is needed to bring about and manage organizational change efficiently and effectively, as Larry Ellison did at Oracle.

As discussed in Chapter 7, the first task facing managers is to establish the structure of task and job reporting relationships that allows organizational members to use resources most efficiently and effectively. Structure alone, however, does not provide the incentive or motivation for people to behave in ways that help achieve organizational goals. The purpose of organizational control is to provide managers with a means of directing and motivating subordinates to work toward achieving organizational goals and to provide managers with specific feedback on how well an organization and its members are performing. Oracle's new control system is intended to direct and motivate employee behavior; changes in its market share, profits, and customer satisfaction ratings are measures that give organizations feedback on how well they are performing.

Organizational structure provides an organization with a skeleton, and control and culture give it the muscles, sinews, nerves, and sensations that allow managers to regulate and govern its activities. The managerial functions of organizing and

controlling are inseparable, and effective managers must learn to make them work together in a harmonious way.

In this chapter, we look in detail at the nature of organizational control and describe the steps in the control process. We discuss three types of control available to managers to control and influence organizational members—output control, behavior control, and clan control (which operates through the values and norms of an organization's culture).² Then, we discuss the important issue of organizational change, change that is possible only when managers have put in place a control system that allows them to alter the way people and groups behave. Finally, we look at the role of entrepreneurs and entrepreneurship in changing the way a company operates. By the end of this chapter, you will appreciate the rich variety of control systems available to managers and understand why developing an appropriate control system is vital to increasing the performance of an organization and its members.

What Is Organizational Control?

As noted in Chapter 1, *controlling* is the process whereby managers monitor and regulate how efficiently and effectively an organization and its members are performing the activities necessary to achieve organizational goals. As discussed in previous chapters, when planning and organizing, managers develop the organizational strategy and structure that they hope will allow the organization to use resources most effectively to create value for customers. In controlling, managers monitor and evaluate whether the organization's strategy and structure are working as intended, how they could be improved, and how they might be changed if they are not working.

Control, however, does not mean just reacting to events after they have occurred. It also means keeping an organization on track, anticipating events that might occur, and then changing the organization to respond to whatever opportunities or threats have been identified. Control is concerned with keeping employees motivated, focused on the important problems confronting the organization, and working together to make the changes that will help an organization perform better over time.

The importance of organizational control

To understand the importance of organizational control, consider how it helps managers obtain superior efficiency, quality, responsiveness to customers, and innovation—the four building blocks of competitive advantage.

To determine how efficiently they are using their resources, managers must be able to accurately measure how many units of inputs (raw materials, human resources, and so on) are being used to produce a unit of output. Managers also must be able to measure how many units of outputs (goods and services) are being produced. A control system contains the measures or yardsticks that allow managers to assess how efficiently the organization is producing goods and services. Moreover, if managers experiment with changing the way the organization produces goods and services to find a more efficient way of producing them, these measures tell managers how successful they have been. For example, when managers at Ford decided to adopt a product team structure to design, engineer, and manufacture new car models, they used measures such as time taken to design a new car and cost savings



A Ford salesperson talks with a prospective car buyer. In the car industry, managers not only need to control the quality of their products but also the quality of their customer service. To improve its customer service, Ford implemented a control system that consists of regularly surveying customers about their experience with particular dealers. If a dealership receives too many complaints, Ford's managers investigate and propose solutions.

per car produced to evaluate how well the new structure worked in comparison with the old structure. They found that the new one performed better. Without a control system in place, managers have no idea how well their organization is performing and how its performance can be improved—information that is becoming increasingly important in today's highly competitive environment.

Today, much of the competition among organizations revolves around increasing the quality of goods and services. In the car industry, for example, cars within each price range compete against one another in features, design, and reliability. Thus, whether a customer will buy a Ford Taurus, GM Malibu, Chrysler Sebring, Toyota Camry, or Honda Accord depends significantly on the quality of each product. Organizational control is important in determining the quality of goods and services because it gives managers feedback on product quality. If the managers of carmakers consistently measure the number

of customer complaints and the number of new cars returned for repairs, or if school principals measure how many students drop out of school or how achievement scores on nationally based tests vary over time, they have a good indication of how much quality they have built into their product—be it an educated student or a car that does not break down. Effective managers create a control system that consistently monitors the quality of goods and services so that they can make continuous improvements to quality—an approach to change that gives them a competitive advantage.

Managers can also help make their organizations more responsive to customers if they develop a control system that allows them to evaluate how well customer-contact employees are performing their jobs, as Oracle now does. Monitoring employee behavior can help managers find ways to increase employees' performance levels, perhaps by revealing areas in which skill training can help employees or by finding new procedures that allow employees to perform their jobs better. When employees know that their behaviors are being monitored, they may also have more incentive to be helpful and consistent in how they act toward customers. To improve customer service, for example, Ford regularly surveys customers about their experiences with particular Ford dealers. If a dealership receives too many customer complaints, Ford's managers investigate the dealership to uncover the sources of the problems and suggest solutions; if necessary, they might even threaten to reduce the number of cars a dealership receives to force the dealer to improve the quality of its customer service.

Finally, controlling can raise the level of innovation in an organization. Successful innovation takes place when managers create an organizational setting in which employees feel empowered to be creative and in which authority is decentralized to employees so that they feel free to experiment and take risks. Deciding on the appropriate control systems to encourage risk taking is an important management challenge; organizational culture (discussed later in this chapter) becomes important in this regard. To encourage product teams at Ford to perform highly, top managers monitored the performance of each team separately—by examining how each team reduced costs or increased quality, for example—and used a bonus system

related to performance to pay each team. The product team manager then evaluated each team member's individual performance, and the most innovative employees received promotions and rewards based on their superior performance.

Control systems and IT

control systems

Formal target-setting, monitoring, evaluation, and feedback systems that provide managers with information about how well the organization's strategy and structure are working.

Control systems are formal target-setting, monitoring, evaluation, and feedback systems that provide managers with information about whether the organization's strategy and structure are working efficiently and effectively.³ Effective control systems alert managers when something is going wrong and give them time to respond to opportunities and threats. An effective control system has three characteristics: It is flexible enough to allow managers to respond as necessary to unexpected events; it provides accurate information and gives managers a true picture of organizational performance; and it provides managers with the information in a timely manner because making decisions on the basis of outdated information is a recipe for failure.

New forms of IT have revolutionized control systems because they facilitate the flow of accurate and timely information up and down the organizational hierarchy and between functions and divisions. Today, employees at all levels of the organization routinely feed information into a company's information system or network and start the chain of events that affect decision making at some other part of the organization. This could be the department store clerk whose scanning of purchased clothing tells merchandise managers what kinds of clothing need to be re-ordered or the salesperson in the field who feeds into a wireless laptop information about customers' changing needs or problems.

feedforward

control Control that allows managers to anticipate problems before they arise.

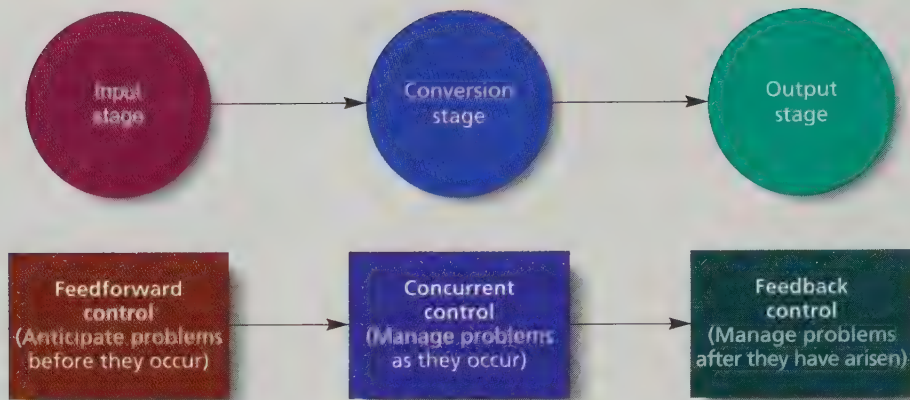
Control and information systems are developed to measure performance at each stage in the process of transforming inputs into finished goods and services (see Figure 8.1). At the input stage, managers use **feedforward control** to anticipate

problems before they arise so that problems do not occur later, during the conversion process.⁴ For example, by giving stringent product specifications to suppliers in advance (a form of performance target), an organization can control the quality of the inputs it receives from its suppliers and thus avoid potential problems during the conversion process. Also, IT can be used to keep in contact with suppliers and to monitor their progress. Similarly, by screening job applicants, often by viewing their résumés electronically, and using several interviews to select the most highly skilled people, managers can lessen the chance that they will hire people who lack the necessary skills or experience to perform effectively. In general, the development of management information systems promotes feedforward control that provides managers with timely information about changes in the task and general environments that may impact their organization later on. Effective managers always monitor trends and changes in the external environment to try to anticipate problems. (We discuss management information systems in detail in Chapter 13.)



Scanning devices, such as the one shown here, are becoming common in all types of work processes, as more companies require real-time information about their products and customers.

Figure 8.1
Three Types of Control



concurrent control

Control that gives managers immediate feedback on how efficiently inputs are being transformed into outputs so that managers can correct problems as they arise.

feedback control

Control that gives managers information about customers' reactions to goods and services so that corrective action can be taken if necessary.

At the conversion stage, **concurrent control** gives managers immediate feedback on how efficiently inputs are being transformed into outputs so that managers can correct problems as they arise. Concurrent control through IT alerts managers to the need to react quickly to whatever is the source of the problem, be it a defective batch of inputs, a machine that is out of alignment, or a worker who lacks the skills necessary to perform a task efficiently. Concurrent control is at the heart of programs to increase quality, in which workers are expected to constantly monitor the quality of the goods or services they provide at every step of the production process and inform managers as soon as they discover problems. One of the strengths of Toyota's production system, for example, is that individual workers are given the authority to push a button to stop the assembly line whenever they discover a quality problem. When all problems have been corrected, the result is a finished product that is much more reliable.

At the output stage, managers use **feedback control** to provide information about customers' reactions to goods and services so that corrective action can be taken if necessary. For example, a feedback control system that monitors the number of customer returns alerts managers when defective products are being produced, and a management information system that measures increases or decreases in relative sales of different products alerts managers to changes in customer tastes so that they can increase or reduce the production of specific products.

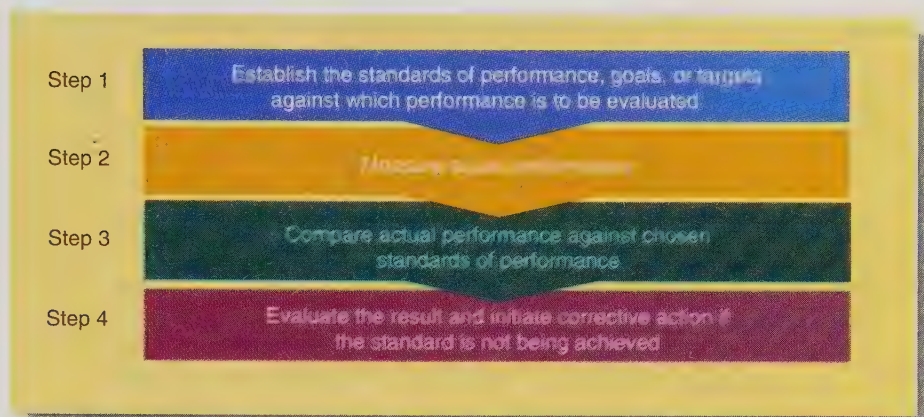
The control process

The control process, whether at the input, conversion, or output stage, can be broken down into four steps: establishing standards of performance, and then measuring, comparing, and evaluating actual performance (see Figure 8.2).⁵

- Step 1: *Establish the standards of performance, goals, or targets against which performance is to be evaluated.*

At step 1 in the control process managers decide on the standards of performance, goals, or targets that they will use in the future to evaluate the performance of the entire organization or part of it (such as a division, a function, or an individual). The standards of performance that managers select measure efficiency, quality, responsiveness to customers, and innovation.⁶ If managers decide to pursue a low-cost strategy, for example, then they need to measure efficiency at all levels in the organization.

Figure 8.2
Four Steps in
Organizational
Control



At the corporate level, a standard of performance that measures efficiency is operating costs, the actual costs associated with producing goods and services, including all employee-related costs. Top managers might set a corporate goal of “reducing operating costs by 10 percent for the next three years” to increase efficiency. Corporate managers might then evaluate divisional managers for their ability to reduce operating costs within their respective divisions, and divisional managers might set cost-savings targets for functional managers. Thus, performance standards selected at one level affect those at the other levels, and ultimately the performance of individual managers is evaluated in terms of their ability to reduce costs. For example, in 2001, struggling Xerox Corp. named Anne Mulcahy as CEO and gave her the challenging task of turning around the company’s fortunes. She was selected because of her 25-year reputation as a person who had been highly successful in reducing costs and increasing efficiency in Xerox’s general markets division.⁷ By 2004, Mulcahy had succeeded; Xerox began to make a profit again as it now could make the products customers wanted.

The number of standards of performance that an organization’s managers use to evaluate efficiency, quality, and so on, can run into the thousands or hundreds of thousands. Managers at each level are responsible for selecting those standards that will best allow them to evaluate how well the part of the organization they are responsible for is performing.⁸ Managers must be careful to choose the standards of performance that allow them to assess how well they are doing with all four of the building blocks of competitive advantage. If managers focus on just one (such as efficiency) and ignore others (such as determining what customers really want and innovating a new line of products to satisfy them), managers may end up hurting their organization’s performance.

- Step 2: *Measure actual performance.*

Once managers have decided which standards or targets they will use to evaluate performance, the next step in the control process is to measure actual performance. In practice, managers can measure or evaluate two things: (1) the actual *outputs* that result from the behavior of their members and (2) the *behaviors* themselves (hence the terms *output control* and *behavior control* used below).⁹

Sometimes both outputs and behaviors can be easily measured. Measuring outputs and evaluating behavior is relatively easy in a fast-food restaurant, for example, because employees are performing routine tasks. Managers of a fast-food

restaurant can quite easily measure outputs by counting how many customers their employees serve and how much money customers spend. Managers can easily observe each employee's behavior and quickly take action to solve any problems that may arise.

When an organization and its members perform complex, nonroutine activities that are intrinsically difficult to measure, it is much more difficult for managers to measure outputs or behavior.¹⁰ It is very difficult, for example, for managers in charge of R&D departments at Merck or Microsoft to measure performance or to evaluate the performance of individual members because it can take 5 or 10 years to determine whether the new products that scientists are developing are going to be profitable. Moreover, it is impossible for a manager to measure how creative a research scientist is by watching his or her actions.

In general, the more nonroutine or complex organizational activities are, the harder it is for managers to measure outputs or behaviors.¹¹ Outputs, however, are usually easier to measure than behaviors because they are more tangible and objective. Therefore, the first kind of performance measures that managers tend to use are those that measure outputs. Then managers develop performance measures or standards that allow them to evaluate behaviors to determine whether employees at all levels are working toward organizational goals. Some simple behavior measures are (1) do employees come to work on time? and (2) do employees consistently follow the established rules for greeting and serving customers? Each type of output and behavior control and the way it is used at the different organizational levels—corporate, divisional, functional, and individual—is discussed in detail subsequently.

- Step 3: *Compare actual performance against chosen standards of performance.*

During step 3, managers evaluate whether—and to what extent—performance deviates from the standards of performance chosen in step 1. If performance is higher than expected, managers might decide that they set performance standards too low and may raise them for the next time period to challenge their subordinates.¹² Managers at Japanese companies are well known for the way they try to raise performance in manufacturing settings by constantly raising performance standards to motivate managers and workers to find new ways to reduce costs or increase quality.

However, if performance is too low and standards were not reached, or if standards were set so high that employees could not achieve them, managers must decide whether to take corrective action.¹³ It is easy to take corrective action when the reasons for poor performance can be identified—for instance, high labor costs. To reduce costs, managers can search for low-cost foreign sources of supply, invest more in technology, or implement cross-functional teams. More often, however, the reasons for poor performance are hard to identify. Changes in the environment, such as the emergence of a new global competitor, a recession, or an increase in interest rates, might be the source of the problem. Within an organization, perhaps the R&D function underestimated the problems it would encounter in developing a new product or the extra costs of doing unforeseen research. If managers are to take any form of corrective action, step 4 is necessary.

- Step 4: *Evaluate the result and initiate corrective action (that is, make changes) if the standard is not being achieved.*

The final step in the control process is to evaluate the results and bring about change as appropriate. Whether performance standards have been met or not,

managers can learn a great deal during this step. If managers decide that the level of performance is unacceptable, they must try to change the way work activities are performed to solve the problem. Sometimes, performance problems occur because the work standard was too high—for example, a sales target was too optimistic and impossible to achieve. In this case, adopting more realistic standards can reduce the gap between actual performance and desired performance.

However, if managers determine that something in the situation is causing the problem, then to raise performance they will need to change the way resources are being utilized.¹⁴ Perhaps the latest technology is not being used; perhaps workers lack the advanced training needed to perform at a higher level; perhaps the organization needs to buy its inputs or assemble its products abroad to compete against low-cost rivals; perhaps it needs to restructure itself or reengineer its work processes to increase efficiency.

The simplest example of a control system is the thermostat in a home. By setting the thermostat, you establish the standard of performance with which actual temperature is to be compared. The thermostat contains a sensing or monitoring device, which measures the actual temperature against the desired temperature. Whenever there is a difference between them, the furnace or air-conditioning unit is activated to bring the temperature back to the standard. In other words, corrective action is initiated. This is a simple control system, for it is entirely self-contained and the target (temperature) is easy to measure.

Establishing targets and designing measurement systems is much more difficult for managers because the high level of uncertainty in the organizational environment causes managers to rarely know what might happen. Thus, it is vital for managers to design control systems to alert them to problems so that they can be dealt with before they become threatening. Another issue is that managers are not just concerned about bringing the organization's performance up to some predetermined standard; they want to push that standard forward, to encourage employees at all levels to find new ways to raise performance.

In the following sections, we consider the three most important types of control that managers use to coordinate and motivate employees to ensure they pursue superior efficiency, quality, innovation, and responsiveness to customers: output control, behavior control, and organizational culture or clan control (see Figure 8.3). Managers use all three to govern and regulate organizational activities, no matter what specific organizational structure is in place.

Figure 8.3
Three
Organizational
Control Systems

Type of control	Mechanisms of control
Output control	Financial measures of performance Organizational goals Operating budgets
Behavior control	Direct supervision Management by objectives Rules and standard operating procedures
Organizational culture/clan control	Values Norms Socialization

Output Control

All managers develop a system of output control for their organizations. First, they choose the goals or output performance standards or targets that they think will best measure efficiency, quality, innovation, and responsiveness to customers. Then they measure to see whether the performance goals and standards are being achieved at the corporate, divisional or functional, and individual levels of the organization. The three main mechanisms that managers use to assess output or performance are financial measures, organizational goals, and operating budgets.

Financial measures of performance

Top managers are most concerned with overall organizational performance and use various financial measures to evaluate performance. The most common are profit ratios, liquidity ratios, leverage ratios, and activity ratios. They are discussed below and summarized in Table 8.1.¹⁵

- *Profit ratios* measure how efficiently managers are using the organization's resources to generate profits. *Return on investment (ROI)*, an organization's net income before taxes divided by its total assets, is the most commonly used financial performance measure because it allows managers of one organization to compare performance with that of other organizations. ROI allows managers to assess an organization's competitive advantage. *Gross profit margin* is the difference between the amount of revenue generated by a product and the resources used to produce the product. This measure provides managers with information about how efficiently an organization is utilizing its resources and about how attractive customers find the product. It also provides managers with a way to assess how well an organization is building a competitive advantage.
- *Liquidity ratios* measure how well managers have protected organizational resources to be able to meet short-term obligations. The *current ratio* (current assets divided by current liabilities) tells managers whether they have the resources available to meet the claims of short-term creditors. The *quick ratio* tells whether they can pay these claims without selling inventory.
- *Leverage ratios* such as the *debt-to-assets ratio* and the *times-covered ratio* measure the degree to which managers use debt (borrow money) or equity (issue new shares) to finance ongoing operations. An organization is highly leveraged if it uses more debt than equity, and debt can be very risky when profits fail to cover the interest on the debt.
- *Activity ratios* provide measures of how well managers are creating value from organizational assets. *Inventory turnover* measures how efficiently managers are turning inventory over so that excess inventory is not carried. *Days sales outstanding* provides information on how efficiently managers are collecting revenue from customers to pay expenses.

The objectivity of financial measures of performance is the reason why so many managers use them to assess the efficiency and effectiveness of their organizations. When an organization fails to meet performance standards such as ROI, revenue, or stock price targets, managers know that they must take corrective action. Thus, financial controls tell managers when a corporate reorganization might be

Table 8.1
Four Measures of Financial Performance

Profit Ratios

Return on investment	=	$\frac{\text{net profit before taxes}}{\text{total assets}}$	Measures how well managers are using the organization's resources to generate profits.
Gross profit margin	=	$\frac{\text{sales revenues} - \text{cost of goods sold}}{\text{sales revenues}}$	The difference between the amount of revenue generated from the product and the resources used to produce the product.

Liquidity Ratios

Current ratio	=	$\frac{\text{current assets}}{\text{current liabilities}}$	Do managers have resources available to meet claims of short-term creditors?
Quick ratio	=	$\frac{\text{current assets} - \text{inventory}}{\text{current liabilities}}$	Can managers pay off claims of short-term creditors without selling inventory?

Leverage Ratios

Debt-to-assets ratio	=	$\frac{\text{total debt}}{\text{total assets}}$	To what extent have managers used borrowed funds to finance investments?
Times-covered ratio	=	$\frac{\text{profit before interest and taxes}}{\text{total interest charges}}$	Measures how far profits can decline before managers cannot meet interest charges. If ratio declines to less than 1, the organization is technically insolvent.

Activity Ratios

Inventory turnover	=	$\frac{\text{cost of goods sold}}{\text{inventory}}$	Measures how efficiently managers are turning inventory over so that excess inventory is not carried.
Days sales outstanding	=	$\frac{\text{current accounts receivable}}{\text{sales for period}} \div \text{days in period}$	Measures how efficiently managers are collecting revenues from customers to pay expenses.

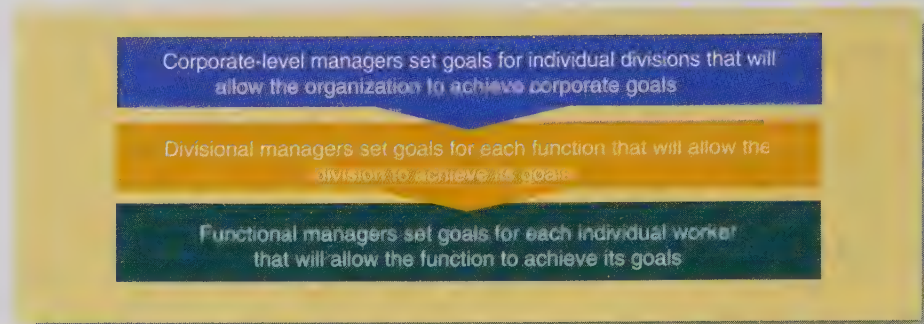
necessary, when they should sell off divisions and exit from businesses, or when they should rethink their corporate-level strategies.¹⁶

Although financial information is an important output control, financial information by itself does not provide managers with all the information they need about the four building blocks of competitive advantage. Financial results inform managers about the results of decisions they have already made; they do not tell managers how to find new opportunities to build competitive advantage in the future. To encourage a future-oriented approach, top managers must establish organizational goals that encourage middle and first-line managers to achieve superior efficiency, quality, innovation, and responsiveness to customers.

Organizational goals

Once top managers consult with lower-level managers and set the organization's overall goals, they establish performance standards for the divisions and functions.

Figure 8.4
Organizationwide
Goal Setting



These standards specify for divisional and functional managers the level at which their units must perform if the organization is to achieve its overall goals.¹⁷ Each division is given a set of specific goals to achieve (see Figure 8.4). For example, former General Electric CEO Jack Welch and his successor Jeffrey Immelt have declared that the goal of each division is to be first or second in its industry in profit. Divisional managers then develop a business-level strategy (based on achieving superior efficiency or innovation) that they hope will allow them to achieve that goal.¹⁸ In consultation with functional managers, they specify the functional goals that the managers of different functions need to achieve to allow the division to achieve its goals. For example, sales managers might be evaluated for their ability to increase sales; materials management managers, for their ability to increase the quality of inputs or lower their costs; R&D managers, for the number of products they innovate or the number of patents they receive. In turn, functional managers establish goals that first-line managers and nonmanagerial employees need to achieve to allow the function to achieve its goals.

Output control is used at every level of the organization, and it is vital that the goals set at each level harmonize with the goals set at other levels so that managers and other employees throughout the organization work together to attain the corporate goals that top managers have set.¹⁹ It is also important that goals be set appropriately so that managers are motivated to accomplish them. If goals are set at an impossibly high level, managers might work only half-heartedly to achieve them because they are certain they will fail. In contrast, if goals are set so low that they are too easy to achieve, managers will not be motivated to use all their resources as efficiently and effectively as possible. Research suggests that the best goals are *specific, difficult goals*—goals that challenge and stretch managers' ability but are not out of reach and do not require an impossibly high expenditure of managerial time and energy. Such goals are often called *stretch goals*.

Deciding what is a specific, difficult goal and what is a goal that is too difficult or too easy is a skill that managers must develop. Based on their own judgment and work experience, managers at all levels must assess how difficult a certain task is, and they must assess the ability of a particular subordinate manager to achieve the goal. If they do so successfully, challenging, interrelated goals—goals that reinforce one another and focus on achieving overall corporate objectives—will energize the organization.

Operating budgets

operating budget

A budget that states how managers intend to use organizational resources to achieve organizational goals.

Once managers at each level have been given a goal or target to achieve, the next step in developing an output control system is to establish operating budgets that regulate how managers and workers attain their goals. An **operating budget** is a blueprint that states how managers intend to use organizational resources to achieve organizational goals efficiently. Typically, managers at one level allocate to subordinate managers a specific amount of resources to use to produce goods and services. Once they have been given a budget, these lower-level managers must decide how to allocate money for different organizational activities. They are then evaluated for their ability to stay within the budget and to make the best use of available resources. For example, managers at GE's washing machine division might have a budget of \$50 million to spend on developing and selling a new line of washing machines. They must decide how much money to allocate to the various functions such as R&D, engineering, and sales so that the division generates the most customer revenue and makes the biggest profit.

Large organizations often treat each division as a singular or stand-alone responsibility center. Corporate managers then evaluate each division's contribution to corporate performance. Managers of a division may be given a fixed budget for resources and be evaluated on the amount of goods or services they can produce using those resources (this is a *cost* or *expense* budget approach). Or managers may be asked to maximize the revenues from the sales of goods and services produced (a *revenue* budget approach). Or managers may be evaluated on the difference between the revenues generated by the sales of goods and services and the budgeted cost of making those goods and services (a *profit* budget approach). Japanese companies' use of operating budgets and challenging goals to increase efficiency is instructive in this context.

In summary, three components—objective financial measures, challenging goals and performance standards, and appropriate operating budgets—are the essence of effective output control. Most organizations develop sophisticated output control systems to allow managers at all levels to keep an accurate account of the organization so that they can move quickly to take corrective action as needed.²⁰ Output control is an essential part of management. The way in which Wal-Mart is using output control to expand internationally is discussed in the following “Managing Globally.”



Managing Globally

Wal-Mart Uses Output Control to Expand Internationally

Retailing giant Wal-Mart has been aggressively expanding internationally in recent years to raise its performance. After moving into Mexico and Europe in the last decade, it began to contemplate entering the Japanese market. An opportunity arose in 2004 when Japan's third-largest supermarket chain, Daiei, which had been losing money for years and was heavily in debt, was put up for sale. Why was a supermarket chain in one of the world's most lucrative markets struggling?

Unlike efficient Japanese carmakers, which employ state-of-the-art IT-based output control systems to collect the detailed information needed to increase their efficiency, Japan's retailers had lagged behind in adopting the new systems. A major reason for this was historical. Until the 1990s, Japan's Large Scale Retail

Store Law allowed small Japanese retailers to block the opening of large, efficient new stores in their neighborhoods for 10 years or more. Although the Japanese government weakened the law so that local storeowners could delay a store opening for only 18 months, there was no history of low-cost competition in the Japanese retail market. So retailers, such as supermarket chains, had never been forced to develop output controls to become more efficient.

A second reason for Daiei's problems revolved around Japan's system of distributing Japanese products. Traditionally, Japanese manufacturers sold their products only by means of wholesalers with which they had developed long-term business relationships. Because the wholesalers added their own price markup and controlled distribution, this made it much more difficult for supermarkets to compete on price and lowered competition. Less competition reduced the incentive for Japanese retailers to invest in materials management output control systems to increase their efficiency.

In contrast, Wal-Mart's focus on developing sophisticated output controls to monitor all aspects of its purchasing and sales activities made it the most efficient U.S. discount retailer in the 1990s. In fact, its skills in materials management allowed it to enter the U.S. supermarket industry and become a major competitor. So, in 2004, to further its global expansion, Wal-Mart was contemplating the purchase of Daiei. Its managers believed that if Wal-Mart transplanted its proprietary IT-based output control systems into Daiei's operations, it could increase

Daiei's efficiency by so much that the supermarket chain would become a highly profitable business. Wal-Mart's other plans for Daiei included purchasing lower-priced goods from abroad in order to pursue a low-cost strategy. Thus, Wal-Mart's global control system, which allows it to identify and purchase products efficiently from manufacturers throughout the world, would help increase Daiei's efficiency.

In the spring of 2005, Wal-Mart was prevented from purchasing Daiei by other Japanese store chains afraid that Wal-Mart would become the strongest competitor in the Japanese retail market and, as it has done in the United States, would force its competitors to adopt state-of-the-art output control systems. Wal-Mart is still pursuing ways to help Daiei and enter the Japanese market, however.



A customer samples a meatball skewer and chats with the owner of a small grocery store in Tokyo. The mom-and-pop shops of Japan's old-style downtown shopping arcades are on shaky ground, facing competition from cheaper mega-outlets of the modern economic world.

Problems with output control

When designing an output control system, managers must be careful to avoid some pitfalls. For example, they must be sure that the output standards they create motivate managers at all levels and do not cause managers to behave in inappropriate ways to achieve organizational goals.

Suppose top managers give divisional managers the goal of doubling profits over a three-year period. This goal seems challenging and reachable when it is jointly agreed upon, and in the first two years profits go up by 70 percent. In the third year, however, an economic recession hits and sales plummet. Divisional managers

think it is increasingly unlikely that they will meet their profit goal. Failure will mean losing the substantial monetary bonus tied to achieving the goal. How might managers behave to try to preserve their bonuses?

One course of action they might take is to find ways to reduce costs, since profit can be increased either by raising revenues or by reducing costs. Thus, divisional managers might cut back on expensive research and development activities, delay maintenance on machinery, reduce marketing expenditures, and lay off middle managers and workers to reduce costs so that at the end of the year they will make their target of doubling profits and receive their bonuses. This tactic might help them achieve a short-run goal—doubling profits—but such actions could hurt long-term profitability or ROI (because a cutback in R&D can reduce the rate of product innovation, a cutback in marketing will lead to the loss of customers, and so on).

Problems of this sort occurred at Gillette when its new chairman, James M. Kilts, announced that the poorly performing company would not be experiencing a turnaround anytime in the near future. He attributed a large part of Gillette's problems to the overly ambitious sales and profit goals that his predecessor had set for managers of its divisions (razors and toiletries, Braun appliances, and Duracell batteries). To achieve these ambitious sales targets, divisional managers had slashed advertising budgets and loaded up on inventory, hoping to sell it quickly and generate large revenues. However, this had backfired when customer demand dropped and a recession occurred.

Kilts saw that Gillette's managers had not been focusing on the right way to reduce costs. Because managers' salaries and bonuses were based on their ability to meet the ambitious goals that had been set for them, they had acted with a short-term mind-set. Managers had not been thinking about the long-term goal of trying to find the best balance between keeping costs under control, keeping customers happy, and keeping the pipeline of new products full.

Kilts announced that henceforth Gillette would no longer provide specific and unrealistic sales and earning targets that created a "circle of doom" and led managers to behave in just the ways that would prevent them from achieving company goals—by reducing advertising to reduce costs, for example. Kilts decided that Gillette would set long-term goals based on carefully drawn marketing plans that targeted products customers wanted and would lead to long-term sales growth. Also, Gillette would carefully examine its product line to focus its resources on products that offered the most payoff and to weed out poorly performing products that did not contribute much to the bottom line. The changes that Kilts made worked; in 2004 Gillette announced record sales and profits.²¹

As Gillette's experience suggests, long-run effectiveness is what managers should be most concerned about. Thus, managers must consider carefully how flexible they should be when using output control. If conditions change (as they will because of uncertainty in the task and general environments), it is probably better for top managers to communicate to managers lower in the hierarchy that they are aware of the changes taking place and are willing to revise and lower goals and standards. Indeed, many organizations schedule yearly revisions of their five-year plan and goals and use scenario planning to avoid the problems Gillette experienced.

The message is clear: Although output control is a useful tool for keeping managers and employees at all levels motivated and the organization on track, it is only a guide to appropriate action. Managers must be sensitive to how they use output control and must constantly monitor its effects at all levels in the organization.

At Oracle, output control was not being used appropriately; Ellison rushed to employ its own sophisticated IT that could collect the data he needed to measure its performance.

Behavior Control

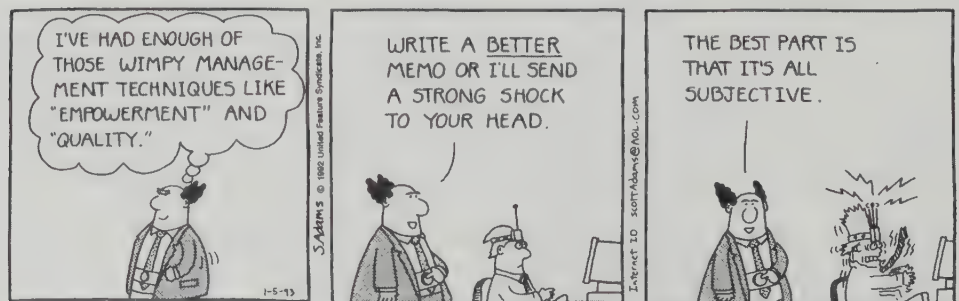
Organizational structure by itself does not provide any mechanism that motivates managers and nonmanagerial employees to behave in ways that make the structure work or even improve the way it works—hence the need for control. Put another way, managers can develop an elegant organizational structure with highly appropriate task and reporting relationships, but it will work as designed only if managers also establish control systems that allow them to motivate and shape employee behavior.²² Output control is one method of motivating employees; behavior control is another method. This section examines three mechanisms of behavior control that managers can use to keep subordinates on track and make organizational structures work as they are designed to work: direct supervision, management by objectives, and rules and standard operating procedures (see Figure 8.3).

Direct supervision

The most immediate and potent form of behavior control is direct supervision by managers who actively monitor and observe the behavior of their subordinates, teach subordinates the behaviors that are appropriate and inappropriate, and intervene to take corrective action as needed. Moreover, when managers personally supervise subordinates, they lead by example and in this way can help subordinates develop and increase their own skill levels. (Leadership is the subject of Chapter 10.) Thus, control through personal supervision can be a very effective way of motivating employees and promoting behaviors that increase efficiency and effectiveness.²³

Nevertheless, certain problems are associated with direct supervision. First, it is very expensive because a manager can personally manage only a small number of subordinates effectively. Therefore, if direct supervision is the main kind of control being used in an organization, a lot of managers will be needed and costs will increase. For this reason, output control is usually preferred to behavior control; indeed, output control tends to be the first type of control that managers at all levels use to evaluate performance.

Second, direct supervision can demotivate subordinates if they feel that they are under such close scrutiny that they are not free to make their own decisions.



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Moreover, subordinates may start to pass the buck and avoid responsibility if they feel that their manager is waiting in the wings ready to reprimand anyone who makes the slightest error.

Third, as noted previously, for many jobs direct supervision is simply not feasible. The more complex a job is, the more difficult it is for a manager to evaluate how well a subordinate is performing. The performance of divisional and functional managers, for example, can be evaluated only over relatively long time periods (this is why an output control system is developed), so it makes little sense for top managers to continually monitor their performance.

Management by objectives

management by objectives (MBO)

A goal-setting process in which a manager and each of his or her subordinates negotiate specific goals and objectives for the subordinate to achieve and then periodically evaluate the extent to which the subordinate is achieving those goals.

To provide a framework within which to evaluate subordinates' behavior and, in particular, to allow managers to monitor progress toward achieving goals, many organizations implement some version of management by objectives. **Management by objectives (MBO)** is a system of evaluating subordinates for their ability to achieve specific organizational goals or performance standards and to meet operating budgets.²⁴ Most organizations make some use of management by objectives because it is pointless to establish goals and then fail to evaluate whether or not they are being achieved. Management by objectives involves three specific steps:

- Step 1: *Specific goals and objectives are established at each level of the organization.*

Management by objective starts when top managers establish overall organizational objectives, such as specific financial performance targets. Then objective setting cascades down throughout the organization as managers at the divisional and functional levels set their objectives to achieve corporate objectives.²⁵ Finally, first-level managers and workers jointly set objectives that will contribute to achieving functional goals.

- Step 2: *Managers and their subordinates together determine the subordinates' goals.*

An important characteristic of management by objectives is its participatory nature. Managers at every level sit down with each of the subordinate managers who report directly to them, and together they determine appropriate and feasible goals for the subordinate and bargain over the budget that the subordinate will need to achieve his or her goals. The participation of subordinates in the objective-setting process is a way of strengthening their commitment to achieving their goals and meeting their budgets.²⁶ Another reason why it is so important for subordinates (both individuals and teams) to participate in goal setting is that doing so enables them to tell managers what they think they can realistically achieve.²⁷

- Step 3: *Managers and their subordinates periodically review the subordinates' progress toward meeting goals.*

Once specific objectives have been agreed on for managers at each level, managers are accountable for meeting those objectives. Periodically, they sit down with their subordinates to evaluate their progress. Normally, salary raises and promotions are linked to the goal-setting process, and managers who achieve their goals receive greater rewards than those who fall short. (The issue of how to design reward systems to motivate managers and other organizational employees is discussed in Chapter 9.)

In the companies that have decentralized responsibility for the production of goods and services to empowered teams and cross-functional teams, management by objectives works somewhat differently. Managers ask each team to develop a set of goals and performance targets that the team hopes to achieve—goals that are consistent with organizational objectives. Managers then negotiate with each team to establish its final goals and the budget the team will need to achieve them. The reward system is linked to team performance, not to the performance of any one team member.

Cypress Semiconductor offers an interesting example of how IT can be used to manage the MBO process quickly and effectively. In the fast-moving semiconductor business a premium is placed on organizational adaptability. At Cypress, CEO T. J. Rodgers was facing a problem. How could he control his growing, 1,500-employee organization without developing a bureaucratic management hierarchy? Rodgers believed that a tall hierarchy hinders the ability of an organization to adapt to changing conditions. He was committed to maintaining a flat and decentralized organizational structure with a minimum of management layers. At the same time, he needed to control his employees to ensure that they perform in a manner consistent with the goals of the company.²⁸ How could he achieve this without resorting to direct supervision and the management hierarchy that it implies?

To solve this problem, Rodgers implemented an online information system through which he can manage what every employee and team is doing in his fast-moving and decentralized organization. Each employee maintains a list of 10 to 15 goals, such as “Meet with marketing for new product launch” or “Make sure to check with customer X.” Noted next to each goal are when it was agreed upon, when it is due to be finished, and whether it has been finished. All of this information is stored on a central computer. Rodgers claims that he can review the goals of all employees in about four hours and that he does so each week.²⁹ How is this possible? He manages by exception and looks only for employees who are falling behind. He then calls them, not to scold but to ask whether there is anything he can do to help them get the job done. It takes only about half an hour each week for employees to review and update their lists. This system allows Rodgers to exercise control over his organization without resorting to the expensive layers of a management hierarchy and direct supervision.

Bureaucratic control

When direct supervision is too expensive and management by objectives is inappropriate, managers might turn to another mechanism to shape and motivate employee behavior: bureaucratic control. **Bureaucratic control** is control by means of a comprehensive system of rules and standard operating procedures (SOPs) that shapes and regulates the behavior of divisions, functions, and individuals. In the appendix to Chapter 1, we discussed Weber’s theory of bureaucracy and noted that all organizations use bureaucratic rules and procedures but some use them more than others.³⁰

Rules and SOPs guide behavior and specify what employees are to do when they confront a problem that needs a solution. It is the responsibility of a manager to develop rules that allow employees to perform their activities efficiently and effectively. When employees follow the rules that managers have developed, their behavior is standardized—actions are performed the same way time and time again—and the outcomes of their work are predictable. And, to the degree that managers can make employees’ behavior predictable, there is no need to monitor the outputs of behavior because standardized behavior leads to standardized outputs.

bureaucratic control Control of behavior by means of a comprehensive system of rules and standard operating procedures.

Suppose a worker at Toyota comes up with a way to attach exhaust pipes that reduces the number of steps in the assembly process and increases efficiency. Always on the lookout for ways to standardize procedures, managers make this idea the basis of a new rule that says, "From now on, the procedure for attaching the exhaust pipe to the car is as follows." If all workers followed the rule to the letter, every car would come off the assembly line with its exhaust pipe attached in the new way and there would be no need to check exhaust pipes at the end of the line. In practice, mistakes and lapses of attention do happen, so output control is used at the end of the line, and each car's exhaust system is given a routine inspection. However, the number of quality problems with the exhaust system is minimized because the rule (bureaucratic control) is being followed.

Service organizations such as retail stores, fast-food restaurants, and home-improvement stores attempt to standardize the behavior of employees by instructing them on the correct way to greet customers or the appropriate way to serve and bag food. Employees are trained to follow the rules that have proved to be most effective in a particular situation, and the better trained the employees are, the more standardized is their behavior and the more trust managers can have that outputs (such as food quality) will be consistent. An interesting example of how creating the wrong rules can reduce performance is discussed in the following "Management Insight."

Management Insight

How to Kill Customer Satisfaction

In the early 2000s, Gateway, the PC maker, saw its customer satisfaction rating plummet from third to fifth in consumer satisfaction with PC makers. This drop caused Gateway's managers considerable anxiety because they used this measure of customer satisfaction as an important indicator of their company's ongoing performance. Such a drop is very serious to a computer maker because the volume of its online sales depends on how easy it is for customers to put their mail-order computer together when it reaches their homes and how easy it is for them to get advice and good service when they encounter a software or hardware problem. Customer satisfaction ratings also directly affect a company's profits, and as Gateway's computer shipments slipped, the company began to lose money.

Why did customer satisfaction plummet? Mike Ritter, director of Gateway consumer marketing, discovered that the source of customer dissatisfaction was a series of new rules and policies the company had instituted for its customer service reps to follow because of its desire to reduce the increasing costs of after-sales service. As Gateway's product line had broadened and many different software and hardware options were made available to customers, the complexity of its customer service procedures had increased. Employees had to have a great deal more information at their disposal to solve customer problems. These problems were often made more serious when customers installed additional software on their computers, which then caused problems with the software already installed on the Gateway machine. As everyone who has installed new software knows, it can take considerable time to iron out the problems and get the new installation to work. Gateway was spending millions of dollars in employee time to solve these problems and desired to reduce this cost.

Ritter discovered that of the 15 rules and procedures the company had instituted for its customer service reps to follow, two rules in particular were the

source of customer dissatisfaction. The first rule concerned the issue of customer-installed software. Gateway had told its service reps to inform customers that if they installed any other software on their machines, this would invalidate Gateway's warranty. This infuriated customers, who asked, Why shouldn't they install other necessary software? The second rule was one that rewarded customer support reps on the basis of how quickly they handled customer calls, meaning that the more calls they handled in an hour or day the higher their bonuses.

The joint effect of these two rules was that customer reps were now motivated to minimize the length of a service call and, in particular, were unwilling to help solve customer problems that resulted from installation of "outlawed software" since doing so took a lot of time. Obviously customers resented this treatment; the result was the big decline in customer satisfaction.

Once Gateway's managers realized the source of the problem, they abolished the 15 rules immediately. Within one month customer satisfaction jumped by over 10 percent. As Gateway's managers discovered, to prevent unexpected problems, it is necessary to carefully choose and evaluate the rules and policies used to control employees' behavior.

In contrast to the situation at Gateway, Dave Lilly, an ex-nuclear submarine commander, chose the *right* rules for siteROCK, a Web hosting company. SiteROCK's business is hosting and managing other companies' Web sites to keep them up and running and error free. A customer's site that goes down or runs haywire is the major enemy. To maximize the performance of his employees and to increase their ability to respond to unexpected online events, Lilly decided that they needed a comprehensive set of rules and standard operating procedures to cover all the major known problems.³¹ Lilly insisted that every problem-solving procedure should be written down. SiteROCK's employees developed over 30 thick binders that list all the processes and checklists they need to follow when an unexpected event happens to solve a specific problem.

Moreover, again drawing from his military experience, Lilly instituted a "two-man rule": Whenever the unexpected happens, each employee must immediately tell a co-worker and the two together should attempt to solve the problem. The goal is simple: Use the rules to achieve a quick resolution of a complex issue. If the existing rules don't work, then employees must experiment, and when they find a solution, the solution is turned into a new rule to be included in the procedures book to aid the future decision making of all employees in the organization.

Problems with bureaucratic control

Like all organizations, siteROCK makes extensive use of bureaucratic control because rules and SOPs effectively control routine organizational activities. With a bureaucratic control system in place, managers can manage by exception and intervene and take corrective action only when necessary. However, managers need to be aware of a number of problems associated with bureaucratic control, because such problems can reduce organizational effectiveness.³²

First, establishing rules is always easier than discarding them. Organizations tend to become overly bureaucratic over time as managers do everything according to the rule book. If the amount of red tape becomes too great, decision making slows and managers react slowly to changing conditions. This sluggishness can imperil an

organization's survival if agile new competitors emerge. Once a siteROCK employee has found a better rule, the old one is discarded.

Second, because rules constrain and standardize behavior and lead people to behave in predictable ways, there is a danger that people become so used to automatically following rules that they stop thinking for themselves. Thus, too much standardization can actually reduce the level of learning taking place in an organization and get the organization off track if managers and workers focus on the wrong issues. An organization thrives when its members are constantly thinking of new ways to increase efficiency, quality, and customer responsiveness. By definition, new ideas do not come from blindly following standardized procedures. Similarly, the pursuit of innovation implies a commitment by managers to discover new ways of doing things; innovation, however, is incompatible with the use of extensive bureaucratic control.

Managers must therefore be sensitive about the way they use bureaucratic control. It is most useful when organizational activities are routine and well understood and when employees are making programmed decisions—for example, in mass-production settings such as Ford or in routine service settings such as stores like Target or Midas Muffler. Bureaucratic control is much less useful in situations where nonprogrammed decisions have to be made and managers have to react quickly to changes in the organizational environment.

organizational culture

The set of values, norms, standards of behavior, and common expectations that controls the ways in which individuals and groups in an organization interact with one another and work to achieve organizational goals.

clan control

The control exerted on individuals and groups in an organization by shared values, norms, standards of behavior, and expectations.

To use output control and behavior control, managers must be able to identify the outcomes they want to achieve and the behaviors they want employees to perform to achieve those outcomes. For many of the most important and significant organizational activities, however, output control and behavior control are inappropriate for several reasons:

- A manager cannot evaluate the performance of workers such as doctors, research scientists, or engineers by observing their behavior on a day-to-day basis.
- Rules and SOPs are of little use in telling a doctor how to respond to an emergency situation or a scientist how to discover something new.
- Output controls such as the amount of time a surgeon takes for each operation or the costs of making a discovery are very crude measures of the quality of performance.

How can managers attempt to control and regulate the behavior of their subordinates when personal supervision is of little use, when rules cannot be developed to tell employees what to do, and when outputs and goals cannot be measured at all or can be measured usefully only over long periods? One source of control increasingly being used by organizations is a strong organizational culture.

Organizational Culture and Clan Control

Organizational culture is another important control system that regulates and governs employee attitudes and behavior. As we discussed in Chapter 2, **organizational culture** is the shared set of beliefs, expectations, values, norms, and work routines that influences how members of an organization relate to one another and work together to achieve organizational goals. **Clan control** is the control exerted on individuals and groups in an organization by shared values, norms, standards of behavior, and

expectations. Organizational culture is not an externally imposed system of constraints, such as direct supervision or rules and procedures. Rather, employees internalize organizational values and norms and then let these values and norms guide their decisions and actions. Just as people in society at large generally behave in accordance with socially acceptable values and norms—such as the norm that people should line up at the checkout counters in supermarkets—so are individuals in an organizational setting mindful of the force of organizational values and norms.

Organizational culture is an important source of control for two reasons. First, it makes control possible in situations where managers cannot use output or behavior control. Second, and more important, when a strong and cohesive set of organizational values and norms is in place, employees focus on thinking about what is best for the organization in the long run—all their decisions and actions become oriented toward helping the organization perform well. For example, a teacher spends personal time after school coaching and counseling students; an R&D scientist works 80 hours a week, evenings, and weekends to help speed up a late project; a salesclerk at a department store runs after a customer who left a credit card at the cash register. An interesting example of a company that has built a strong culture based on close attention to developing the right set of output and behavior controls is UPS, profiled in the following “Manager as a Person.”



Manager as a Person

James Casey Creates a Culture for UPS

United Parcel Service (UPS) controls more than three-fourths of the ground and air parcel service in the United States, delivering over 10 million packages a day in its fleet of 150,000 trucks.³³ It is also the most profitable company in its industry. UPS employs over 250,000 people, and since its founding as a bicycle-messenger service in 1907 by James E. Casey, UPS has developed a culture that has been a model for competitors such as FedEx and the U.S. Postal Service.

From the beginning, Casey made efficiency and economy the company's driving values and loyalty, humility, discipline, dependability, and intense effort the key norms and standards UPS employees should adopt. UPS has always gone to extraordinary lengths to develop and maintain these values and norms in its workforce.

First, its operating systems from the top of the company down to its trucking operations are the subject of intense scrutiny by the company's 3,000 industrial engineers. These engineers are constantly on the lookout for ways to measure outputs and behaviors to improve efficiency. They time every part of an employee's job. Truck drivers, for example, are instructed in extraordinary detail on how to perform their tasks: They must step from their truck with their right foot first, fold their money face-up, carry packages under their left arm, walk at a pace of 3 feet per second, and slip the key ring holding their truck keys over their third finger.³⁴ Employees are not allowed to have beards, must be carefully groomed, and are instructed in how to deal with customers. Drivers who perform below average receive visits from training supervisors who accompany them on their delivery routes and instruct them on how to raise their performance level. Not surprisingly, as a result of this intensive training and close behavior control, UPS employees internalize the company's strong norms



UPS drivers must follow strict guidelines regarding appearance, job performance, and customer interactions.

about the appropriate ways to behave to help the organization achieve its values of economy and efficiency.

Its search to find the best set of output controls leads UPS to constantly develop and introduce the latest in IT into the company's operations, particularly its materials management operations. In fact, today UPS offers a consulting service to other companies in the area of global supply chain management. Its goal is to teach other companies how to pursue its values of efficiency and economy, values that the company has been pursuing for the last hundred years as a result of the values of its founder.

Adaptive cultures versus inert cultures

Many researchers and managers believe that employees of some organizations go out of their way to help the organization because it has a strong and cohesive organizational culture—an *adaptive culture* that controls employee attitudes and behaviors. Adaptive cultures, such as that at UPS, are cultures whose values and norms help an organization to build momentum and to grow and change as needed to achieve its goals and be effective. By contrast, *inert cultures* are those that lead to values and norms that fail to motivate or inspire employees; they lead to stagnation and often failure over time. What leads to an adaptive or inert culture?

Researchers have found that organizations with strong adaptive cultures, like 3M, UPS, Microsoft, and IBM, invest in their employees. They demonstrate their commitment to their members by, for example, emphasizing the long-term nature of the employment relationship and trying to avoid layoffs. These companies develop long-term career paths for their employees and invest heavily in training and development to increase employees' value to the organization. In these ways, terminal and instrumental values pertaining to the worth of human resources encourage the development of supportive work attitudes and behaviors.

In adaptive cultures employees often receive rewards linked directly to their performance and to the performance of the company as a whole. Sometimes, employee stock ownership plans (ESOPs) are developed in which workers as a group are allowed to buy a significant percentage of their company's stock. Workers who are owners of the company have additional incentive to develop skills that allow them to perform highly and search actively for ways to improve quality, efficiency, and performance. At Dell, for example, employees are able to buy Dell stock at a steep (15 percent) discount; this allows them to build a sizable stake in the company over time.

Some organizations, however, develop cultures with values that do not include protecting and increasing the worth of their human resources as a major goal. Their employment practices are based on short-term employment according to the needs of the organization and on minimal investment in employees who perform simple, routine tasks. Moreover, employees are not often rewarded based on their performance and thus have little incentive to improve their skills or otherwise invest in the organization to help it to achieve goals. If a company has an inert culture, poor

working relationships frequently develop between the organization and its employees, and instrumental values of noncooperation, laziness, and loafing and work norms of output restriction are common.

Moreover, an adaptive culture develops an emphasis on entrepreneurship and respect for the employee and allows the use of organizational structures, such as the cross-functional team structure, that empower employees to make decisions and motivate them to succeed. By contrast, in an inert culture, employees are content to be told what to do and have little incentive or motivation to perform beyond minimum work requirements. As you might expect, the emphasis is on close supervision and hierarchical authority, which result in a culture that makes it difficult to adapt to a changing environment.

Nokia, the world's largest wireless phone maker, headquartered in Finland, is a good example of a company in which managers strived to create an adaptive culture.³⁵ Nokia's president, Matti Alahuhta, believes that Nokia's cultural values are based on the Finnish character: Finns are down-to-earth, rational, straightforward people. They are also very friendly and democratic people who do not believe in a rigid hierarchy based either on a person's authority or on social class. Nokia's culture reflects these values because innovation and decision making are pushed right down to the bottom line, to teams of employees who take up the challenge of developing the ever-smaller and more sophisticated phones for which the company is known. Bureaucracy is kept to a minimum at Nokia; its adaptive culture is based on informal and personal relationships and norms of cooperation and teamwork.

To help strengthen its culture, Nokia has built a futuristic open-plan steel and glass building just outside Helsinki. Here, in an open environment, its research and development people can work together to innovate new kinds of wireless phones. More than one out of every three of Nokia's 60,000 employees work in research; what keeps these people together and focused is Nokia's company mission to produce phones that are better, cheaper, smaller, and easier to use than competitor's phones.³⁶

This is the "Nokia Way," a system of cultural values and norms that can't be written down but is always present in the values that cement people together and in the language and stories that its members use to orient themselves to the company.

Another company with an adaptive culture is Merck & Co., one of the largest producers of prescription drugs in the world. Much of Merck's success can be attributed to its ability to attract the very best research scientists, who come because its adaptive culture nurtures scientists and emphasizes values and norms of innovation. Scientists are given great freedom to pursue intriguing ideas even if the commercial



An aerial view of the cafeteria at Nokia's headquarters in Espoo, Finland. The open architecture of the building reflects the company's culture, which is based on informal and personal relationships and norms of cooperation and teamwork.

payoff is questionable. Moreover, researchers are inspired to think of their work as a quest to alleviate human disease and suffering worldwide, and Merck has a reputation as an ethical company whose values put people above profits.

Although the experience of Nokia and Merck suggests that organizational culture can give rise to managerial actions that ultimately benefit the organization, this is not always the case. The cultures of some organizations become dysfunctional, encouraging managerial actions that harm the organization and discouraging actions that might lead to an improvement in performance.³⁷ For example, Sunflower Electric Power Corporation, a generation and transmission cooperative, almost went bankrupt in the early 2000s. A state committee of inquiry that was set up to find the source of the problem put the blame on Sunflower's CEO. The committee decided that he had created an abusive culture based on fear and blame that encouraged managers to fight over and protect their turf—an inert culture. Managers were afraid to rock the boat or make suggestions since they could not predict what would happen to them.

The CEO was fired and a new CEO, Chris Hauck, was appointed to change the cooperative's culture. He found it very hard to do so as his senior managers were so used to the old values and norms. One top manager, for example, engaged so frequently in the practice of berating one supervisor that the man became physically sick.³⁸ Hauck fired this manager and other managers as a signal that such behavior would no longer be tolerated. With the help of consultants, he went about the slow process of changing values and norms to emphasize cooperation, teamwork, and respect for others. Clearly, managers can influence the way their organizational culture develops over time, often in a short period of time.

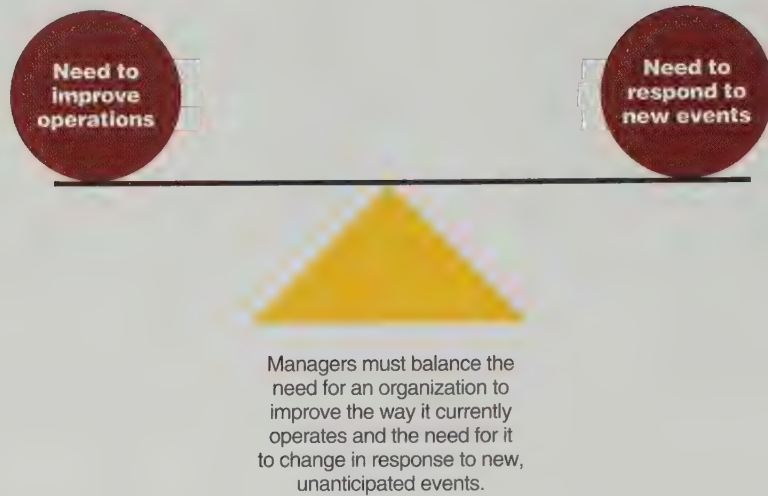
Organizational Change

As we have discussed above, many problems can arise if an organization's control systems are not designed correctly. One of these problems is that an organization cannot change or adapt in response to a changing environment unless it has effective control over its activities. Companies can lose this control over time, as happened to Oracle and Gateway, or they can change in ways that make them more effective, as happened to UPS and Wal-Mart.

Interestingly enough, there is a fundamental tension or need to balance two opposing forces in the control process that influences the way organizations change. As just noted, organizations and their managers need to be able to control their activities and make their operations routine and predictable. At the same time, however, organizations have to be responsive to the need to change, and managers and employees have to “think on their feet” and realize when they need to depart from routines to be responsive to unpredictable events. In other words, even though adopting the right set of output and behavior controls is essential for improving efficiency, because the environment is dynamic and uncertain, employees also need to feel that they have the autonomy to depart from routines as necessary to increase effectiveness. (See Figure 8.5.)

It is for this reason that many researchers believe that the highest-performing organizations are those that are constantly changing—and thus become experienced at doing so—in their search to become more efficient and effective. And companies like UPS, and more recently Oracle, are constantly changing the mix of their activities to move forward even as they are seeking to make their existing operations more efficient. For example, UPS entered the air express parcel market, bought a

Figure 8.5
Organizational
Control and
Change



chain of mailbox stores, and began offering a consulting service. At the same time, it has been increasing the efficiency of its ground transport network.

The need to constantly search for ways to improve efficiency and effectiveness makes it vital that managers develop the skills necessary to manage change effectively. Several experts have proposed a model that managers can follow to implement change successfully.⁴⁰ **Organization change** is the movement of an organization away from its present state and toward some desired future state to increase its efficiency and effectiveness. Figure 8.6 outlines the steps that managers must take to manage change effectively. In the rest of this section we examine each one.

organization change The movement of an organization away from its present state and toward some desired future state to increase its efficiency and effectiveness.

Assessing the need for change

Organizational change can affect practically all aspects of organizational functioning, including organizational structure, culture, strategies, control systems, and groups and teams, as well as the human resource management system and critical organizational processes such as communication, motivation, and leadership. Organizational change can bring alterations in the ways managers carry out the critical tasks of planning, organizing, leading, and controlling and the ways they perform their managerial roles.

Deciding how to change an organization is a complex matter because change disrupts the status quo and poses a threat, prompting employees to resist attempts to alter work relationships and procedures. *Organizational learning*, the process through which managers try to increase organizational members' abilities to understand and appropriately respond to changing conditions, can be an important impetus for change and can help all members of an organization, including managers, effectively make decisions about needed changes.

Assessing the need for change calls for two important activities: recognizing that there is a problem and identifying its source. Sometimes the need for change is obvious, such as when an organization's performance is suffering. Often, however, managers have trouble determining that something is going wrong because problems develop gradually; organizational performance may slip for a number of years before a problem becomes obvious. Thus, during the first step in the change process, managers need to recognize that there is a problem that requires change.

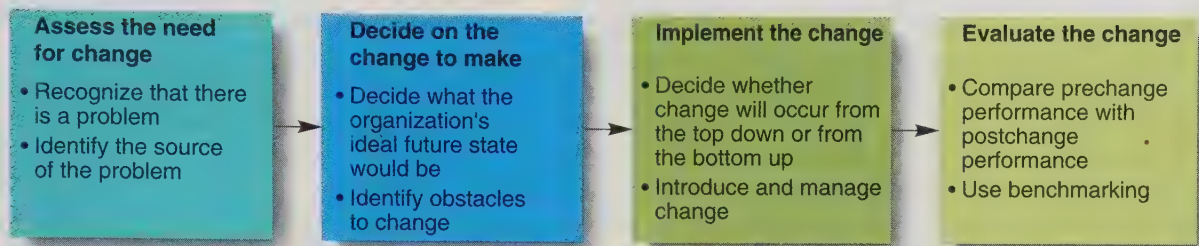


Figure 8.6
Four Steps in the Organizational Change Process

Often the problems that managers detect have produced a gap between desired performance and actual performance. To detect such a gap, managers need to look at performance measures—such as falling market share or profits, rising costs, or employees' failure to meet their established goals or stay within budgets—which indicate whether change is needed. These measures are provided by organizational control systems, discussed earlier in the chapter.

To discover the source of the problem, managers need to look both inside and outside the organization. Outside the organization, they must examine how changes in environmental forces may be creating opportunities and threats that are affecting internal work relationships. Perhaps the emergence of low-cost competitors abroad has led to conflict among different departments that are trying to find new ways to gain a competitive advantage. Managers also need to look within the organization to see whether its structure is causing problems between departments. Perhaps a company does not have integrating mechanisms in place to allow different departments to respond to low-cost competition.

Deciding on the change to make

Once managers have identified the source of the problem, they must decide what they think the organization's ideal future state would be. In other words, they must decide where they would like their organization to be in the future—what kinds of goods and services it should be making, what its business-level strategy should be, how the organizational structure should be changed, and so on. During this step, managers also must engage in planning how they are going to attain the organization's ideal future state.

This step in the change process also includes identifying obstacles or sources of resistance to change. Managers must analyze the factors that may prevent the company from reaching its ideal future state. Obstacles to change are found at the corporate, divisional, departmental, and individual levels of the organization.

Corporate-level changes in an organization's strategy or structure, even seemingly trivial changes, may significantly affect how divisional and departmental managers behave. Suppose that to compete with low-cost foreign competitors, top managers decide to increase the resources spent on state-of-the-art machinery and reduce the resources spent on marketing or R&D. The power of manufacturing managers would increase, and the power of marketing and R&D managers would fall. This decision would alter the balance of power among departments and might lead to increased conflict as departments start fighting to retain their status in the organization. An organization's present strategy and structure are powerful obstacles to change.

Whether a company's culture is adaptive or inert facilitates or obstructs change. Organizations with entrepreneurial, flexible cultures, such as high-tech companies, are much easier to change than are organizations with more rigid cultures, such as those sometimes found in large, bureaucratic organizations like the military or General Motors.

The same obstacles to change exist at the divisional and departmental levels as well. Division managers may differ in their attitudes toward the changes that top managers propose and, if their interests and power seem threatened, will resist those changes. Managers at all levels usually fight to protect their power and control over resources. Given that departments have different goals and time horizons, they may also react differently to the changes that other managers propose. When top managers are trying to reduce costs, for example, sales managers may resist attempts to cut back on sales expenditures if they believe that problems stem from manufacturing managers' inefficiencies.

At the individual level, too, people are often resistant to change because change brings uncertainty and uncertainty brings stress. For example, individuals may resist the introduction of a new technology because they are uncertain about their abilities to learn it and effectively use it.

These obstacles make organizational change a slow process. Managers must recognize the potential obstacles to change and take them into consideration. Some obstacles can be overcome by improving communication so that all organizational members are aware of the need for change and of the nature of the changes being made. Empowering employees and inviting them to participate in the planning for change also can help overcome resistance and allay employees' fears. In addition, managers can sometimes overcome resistance by emphasizing group or shared goals such as increased organizational efficiency and effectiveness. The larger and more complex an organization is, the more complex is the change process.

Implementing the change

Generally, managers implement—that is, introduce and manage—change from the top down or from the bottom up.⁴¹ **Top-down change** is implemented quickly: Top managers identify the need for change, decide what to do, and then move quickly to implement the changes throughout the organization. For example, top managers may decide to restructure and downsize the organization and then give divisional and departmental managers specific goals to achieve. With top-down change, the emphasis is on making the changes quickly and dealing with problems as they arise; it is revolutionary in nature, such as the change that took place at Oracle.

Bottom-up change is typically more gradual or evolutionary. Top managers consult with middle and first-line managers about the need for change. Then, over time, managers at all levels work to develop a detailed plan for change. A major advantage of bottom-up change is that it can co-opt resistance to change from employees. Because the emphasis in bottom-up change is on participation and on keeping people informed about what is going on, uncertainty and resistance are minimized.

Evaluating the change

The last step in the change process is to evaluate how successful the change effort has been in improving organizational performance.⁴² Using measures such as

top-down change

A fast, revolutionary approach to change in which top managers identify what needs to be changed and then move quickly to implement the changes throughout the organization.

bottom-up change

A gradual or evolutionary approach to change in which managers at all levels work together to develop a detailed plan for change.

benchmarking The process of comparing one company's performance on specific dimensions with the performance of other, high-performing organizations.

changes in market share, in profits, or in the ability of managers to meet their goals, managers compare how well an organization is performing after the change with how well it was performing before. Managers also can use **benchmarking**, comparing their performance on specific dimensions with the performance of high-performing organizations to decide how successful a change effort has been. For example, when Xerox was doing poorly in the 1980s, it benchmarked the efficiency of its distribution operations against that of L. L. Bean, the efficiency of its central computer operations against that of John Deere, and the efficiency of its marketing abilities against that of Procter & Gamble. Those three companies are renowned for their skills in these different areas, and by studying how they performed, Xerox was able to dramatically increase its own performance. Benchmarking is a key tool in total quality management, an important change program discussed in Chapter 14.

In summary, organizational control and change are closely linked because organizations operate in environments that are constantly changing and so managers must be alert to the need to change their strategies and structures. High-performing organizations are those whose managers are attuned to the need to continually modify the way they operate and that adopt techniques like empowered work groups and teams, benchmarking, and global outsourcing to remain competitive in a global world.

Entrepreneurship, Control, and Change

entrepreneurs people who notice opportunities and take responsibility for mobilizing the resources necessary to produce new and improved goods and services.

As we discussed in Chapter 1, managers are responsible for supervising the use of human and other resources to achieve effective and efficient organizational goals. **Entrepreneurs**, by contrast, are the people who notice opportunities and take responsibility for mobilizing the resources necessary to produce new and improved goods and services. Essentially, entrepreneurs bring about change to companies and industries because they see new and improved ways to use resources to create products customers will want to buy. At the same time, entrepreneurs who start new business ventures are responsible for all the initial planning, organizing, leading, and controlling necessary to make their idea a reality. If their idea is viable and entrepreneurs do attract customers, then their business grows and then they need to hire managers who will take responsibility for organizing and controlling all the specific functional activities such as marketing, accounting, and manufacturing necessary for a growing organization to be successful.

Typically, entrepreneurs assume the substantial risk associated with starting new businesses (many new businesses fail) and they receive all the returns or profits associated with the new business venture. These people are the Bill Gateses, Larry Ellisons, or Liz Claibornes of the world who make vast fortunes when their businesses succeed. Or they are among the millions of people who start new business ventures only to lose their money when their business's fail. Despite the fact that an estimated 80 percent of small businesses fail in the first three to five years, by some estimates 38 percent of men and 50 percent of women in today's workforce want to start their own companies. One entrepreneur who has succeeded is Omar Maden, profiled in the following "Management Insight."



Entrepreneurship at Maden Technologies

In 1962, fifteen-year-old Omar Maden fled Cuba alone and penniless and was resettled with foster parents in Portland, Oregon. Five years later he was drafted into the U.S. Army during the Vietnam War and the former Afro-Cuban Maden found himself working on command and control communications technology for artillery and missiles. At the end of the war, Maden's superior officers encouraged him to remain in the Army because of his considerable technical skills. Maden became an Army information technology expert, and rose up the ranks to become a major. He was transferred to the Pentagon, where he was responsible for implementing some key logistics communications technologies.

After retiring from the Army in the mid-1980s, Maden decided he could use his IT skills to become an independent consultant. Using a home equity loan and his personal savings, he started Maden Technologies. Soon his previous employer, the Army, began to call on his services. Maden's big break came when he was hired to oversee deployment of the Army's logistics center for the Desert Storm campaign during the war with Iraq. He and his team of highly trained IT analysts fashioned a field communications system that offered Desert Storm's commanders instantaneous performance feedback which put them in total control of all mobile military resources. Maden's systems excelled, and his success in managing this venture led to more contracts. Within 10 years Maden Technologies had become one of the Pentagon's largest research and development contractors.

Since 1995, Maden has organized his IT analysts into teams to develop the different communications products that the Army needs. For example, one team converted the military's internal email system into a battlefield tool that allows everyone to communicate with everyone else. Another team has developed a smart card that will have embedded in it a soldier's complete personal, medical, and military record. These cards were issued to 4 million Army personnel in 2002.

Realizing that his company's technological innovations and skills could be used more widely, Maden has been trying to reposition his company as a technology service provider to industry since the early 2000s. His employees have been pushing him to do this because they have received large stock options for their major contributions and are anxious to see their company succeed at a national level. Moreover, using his military experience, Maden has been careful to assign authority for each project to the managers of the team responsible for developing each product to encourage entrepreneurial team behavior. Team members are given wide authority to make decisions, and each team works closely with its customers—Army officers—so that team members can be sure they are designing a product that matches the Army's current and future needs.

Clearly, entrepreneurship is an ongoing process at Maden Technologies. Maden has taken advantage of the company's IT skills and used them to develop creative solutions for the Army's communications problems, and also for industry. Where Maden Technologies will be in 10 years is an interesting question. Maden and his teams are confident they will soon be able to offer enterprise management solutions that are on a par with those offered by IBM, Computer Associates, and other software giants for a fraction of the cost. When this occurs Maden Technologies will join the ranks of the Fortune 100 and Maden will have achieved the American Dream.

intrapreneurs

employees of existing organizations who notice opportunities for product or service improvements and are responsible for managing the development process.

entrepreneurship

the mobilization of resources to take advantage of an opportunity to provide customers with new or improved goods and services.

As the example of Maden Technologies suggests, entrepreneurship does not just end once a new business is founded. Entrepreneurship carries on inside an organization over time, and many people throughout an organization take responsibility for developing innovative goods and services. For example, managers, scientists, or researchers employed by existing companies engage in entrepreneurial activity when they develop new or improved products. To distinguish these individuals from entrepreneurs who found their own businesses, employees of existing organizations who notice opportunities for product or service improvements and are responsible for managing the development process are known as **intrapreneurs**. In general, then, **entrepreneurship** is the mobilization of resources to take advantage of an opportunity to provide customers with new or improved goods and services; intrapreneurs engage in entrepreneurship within an existing company.

An interesting relationship exists between entrepreneurs and intrapreneurs. Many intrapreneurs become dissatisfied when their superiors decide not to support or to fund new product ideas and development efforts that the intrapreneurs think will succeed. What do intrapreneurs do who feel that they are getting nowhere? Very often intrapreneurs decide to leave their employers and start their own organizations to take advantage of their new product ideas. In other words, intrapreneurs become entrepreneurs and found companies that may compete with the companies they left.

Many of the world's most successful organizations have been started by frustrated intrapreneurs who became entrepreneurs. William Hewlett and David Packard left Fairchild Semiconductor, an early industry leader, when managers of that company would not support Hewlett and Packard's ideas; their company soon outperformed Fairchild. Compaq Computer was founded by Rod Canion and some of his colleagues, who left Texas Instruments (TI) when managers there would not support Canion's idea that TI should develop its own personal computer. To prevent the departure of talented people, organizations need to take steps to promote internal entrepreneurship.

There is also an interesting dynamic between entrepreneurship and management. Very often, it turns out that the entrepreneur who initially founded the business does not have the management skills to successfully control and change the business over time. They may, for example, lack an understanding of how to create the control structure necessary to manage a successful long-term strategy; this was Larry Ellison's problem in the opening case. Entrepreneurs also may not recognize the need to change their companies because they are so close to it; in other words, they "cannot see the forest for the trees"; apparently this was also Ellison's problem.

Frequently a founding entrepreneur lacks the skills, patience, or experience to engage in the difficult and challenging work of management. Some entrepreneurs find it difficult to delegate authority because they are afraid to risk letting others manage their company. As a result, founding entrepreneurs can become overloaded, and the quality of their decision making declines. Other entrepreneurs lack the detailed knowledge necessary to establish state-of-the-art control systems or to create the operations management procedures that are vital to increase the efficiency of their organizations' production systems (discussed in Chapter 14).

In summary, it is necessary to do more than create a new product to succeed; an entrepreneur must hire managers who can create an operating and control system that will allow a new venture to survive and prosper. Very often, venture capitalists, the people who provide the capital to fund a new venture, will loan entrepreneurs the money only if they agree from the outset to let a professional manager become the CEO of the new company. The entrepreneur then holds a senior planning and advisory role in the company, often chairing its board of directors.

Summary and Review

WHAT IS ORGANIZATIONAL CONTROL?

Controlling is the process whereby managers monitor and regulate how efficiently and effectively an organization and its members are performing the activities necessary to achieve organizational goals. Controlling is a four-step process: (1) establishing performance standards, (2) measuring actual performance, (3) comparing actual performance against performance standards, and (4) evaluating the results and initiating corrective action if needed.

OUTPUT CONTROL To monitor output or performance, managers choose goals or performance standards that they think will best measure efficiency, quality, innovation, and responsiveness to customers at the corporate, divisional, departmental or functional, and individual levels. The main mechanisms that managers use to monitor output are financial measures of performance, organizational goals, and operating budgets.

BEHAVIOR CONTROL In an attempt to shape behavior and induce employees to work toward achieving organizational goals, managers utilize direct supervision, management by objectives, and bureaucratic control by means of rules and standard operating procedures.

ORGANIZATIONAL CULTURE AND CLAN CONTROL Organizational culture is the set of values, norms, standards of behavior, and common expectations that control the ways individuals and groups in an organization interact with one another and work to achieve organizational goals. Clan control is the control exerted on individuals and groups by shared values, norms, standards of behavior, and expectations. Organizational culture is transmitted to employees through the values of the founder, the process of socialization, organizational ceremonies and rites, and stories and language. The way managers perform their management functions influences the kind of culture that develops in an organization.

ORGANIZATIONAL CONTROL AND CHANGE There is a need to balance two opposing forces in the control process that influences the way organizations change. On the one hand, managers need to be able to control organizational activities and make their operations routine and predictable. On the other hand, organizations have to be responsive to the need to change, and managers must understand when they need to depart from routines to be responsive to unpredictable events. The four steps in managing change are (1) assessing the need for change, (2) deciding on the changes to make, (3) implementing change, and (4) evaluating the results of change.

ENTREPRENEURSHIP, CONTROL, AND CHANGE Entrepreneurs are people who notice opportunities and collect and mobilize the resources necessary to produce new and improved goods and services. Intrapreneurs are employees in existing companies who notice opportunities to improve the companies' products and become responsible for managing the change process necessary to bring them to market. Both entrepreneurs and intrapreneurs play important roles in the control and change process.



Management in Action

Topics for Discussion and Action

Discussion

1. What is the relationship between organizing and controlling?
2. How do output control and behavior control differ?
3. Why is it important for managers to involve subordinates in the control process?
4. What is organizational culture, and how does it affect the way employees behave?

5. What kind of controls would you expect to find most used in (a) a hospital, (b) the Navy, (c) a city police force. Why?

Action

6. Ask a manager to list the main performance measures that he or she uses to evaluate how well the organization is achieving its goals.
7. Ask the same or a different manager to list the main forms of output control and behavior control that he or she uses to

monitor and evaluate employee behavior.

8. Interview some employees of an organization, and ask them about the organization's values, norms, socialization practices, ceremonies and rites, and special language and stories. Referring to this information, describe the organization's culture.
9. Interview an entrepreneur about how he or she organized a new venture.



Building Management Skills

Understanding Controlling

For this exercise you will analyze the control systems used by a real organization such as a department store, restaurant, hospital, police department, or small business. Your objective is to uncover all the different ways in which managers monitor and evaluate the performance of the organization and employees.

1. At what levels does control take place in this organization?
2. Which output performance standards (such as financial measures and organizational goals) do managers use most often to evaluate performance at each level?
3. Does the organization have a management-by-objectives system in place? If it does, describe it. If it does not, speculate about why not.
4. How important is behavior control in this organization? For example, how much of managers' time is spent directly supervising employees? How formalized is the organization? Do employees receive a book of rules to instruct them about how to perform their jobs?
5. What kind of culture does the organization have? What are the values and norms? What effect does the organizational culture have on the way employees behave or treat customers?
6. Based on this analysis, do you think there is a fit between the organization's control systems and its culture? What is the nature of this fit? How could it be improved?





Small Group Breakout Exercise

How Best to Control the Sales Force?

Form groups of three or four people, and appoint one member as the spokesperson who will communicate your findings to the whole class when called on by the instructor. Then discuss the following scenario.

You are the regional sales managers of an organization that supplies high-quality windows and doors to building supply centers nationwide. Over the last three years, the rate of sales growth has slackened. There is increasing evidence that, to make their jobs easier, salespeople are primarily servicing large customer accounts and ignor-

ing small accounts. In addition, the salespeople are not dealing promptly with customer questions and complaints, and this inattention has resulted in a drop in after-sales service. You have talked about these problems, and you are meeting to design a control system to increase both the amount of sales and the quality of customer service.

1. Design a control system that you think will best motivate salespeople to achieve these goals.
2. What relative importance do you put on (a) output control, (b) behavior control, and (c) organizational culture in this design.



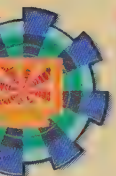
Be the Manager

You have been asked by your company's CEO to find a way to improve the performance of its teams of Web-design and Web-hosting specialists and programmers. Each team works on a different aspect of Web-site production, and while each is responsible for the quality of its own performance, its performance also depends on how well the other teams perform. Your task is to create a control system that will help to increase the performance of each

team separately and facilitate cooperation among the teams. This is necessary because the various projects are interlinked and affect one another just as the different parts of a car must fit together. Since competition in the Web-site production market is intense, it is imperative that each Web site be up and running as quickly as possible and incorporate all the latest advances in Web-site software technology.

Questions

1. What kind of output controls will best facilitate positive interactions both within the teams and among the teams?
2. What kind of behavior controls will best facilitate positive interactions both within the teams and among the teams?
3. How would you go about helping managers develop a culture to promote high team performance?



Additional Activities on the Build Your Management Skills DVD

- **Test Your Knowledge:**
(1) Categories of Managerial Control and (2) Characteristics of Successful Entrepreneurs
- **Self Assessment:** Assessing Your Flexibility
- **Manager's Hot Seat:**
Change: More Pain than Gain

Managing Ethically

Some managers and organizations go to great lengths to monitor their employees' behavior, and they keep extensive records about employees' behavior and performance. Some organizations also seem to possess norms and values that cause their employees to behave in certain ways.

Questions

1. Either by yourself or in a group, think about the ethical implications of organizations' monitoring and collecting information about their employees. What kind of information is it ethical to collect or unethical to collect? Why? Should managers and organizations inform subordinates they are collecting such information?
2. Similarly, some organizations' cultures, like those of Arthur Andersen, the accounting firm, and of Enron, seemed to have developed norms and values that caused their members to behave in unethical ways. When and why does a strong norm that encourages high performance become one that can cause people to act unethically? How can organizations keep their values and norms from becoming "too strong"?



BusinessWeek

Case in the News

The "Constant Challenge" at eBay

Online auction site eBay just finished its annual member conference, eBay Live!, on June 26, bringing together more than 10,000 of its sellers and buyers in New Orleans. It's a chance for the most fanatic of eBay's 45 million active members to trade ideas, take classes in how to sell better, and lobby the online marketplace's staff for changes.

Part love fest and part bitch session, the show is an annual highlight for eBay Chief Executive Margaret C. Whitman, who takes the opportunity to mingle with the masses. As she gazed down on the show floor, Whitman shared her thoughts with *BusinessWeek* Silicon Valley Bureau Chief Robert D. Hof about how she copes with the contentious hordes on eBay and why, despite rumors that she might leave the company before long, she's happy with her job.

Edited excerpts of their conversation follow:

Q: Is it difficult to manage sellers, many of whom seem to have little business experience?

A: Actually, most of these sellers know more about eBay than most [eBay] employees. They use it every single day. They're the experts. Folks have basically quit their day jobs to sell full-time on eBay. They do eBay before their kids come home from school. The businesses that have been built on this platform are remarkable.

Q: Some veteran sellers are fed up with eBay's constant tinkering with the site. How are you responding?

A: The community right now has seen a lot of change. We probably need to slow down that pace of change just a tad. It's hard for folks to adapt to so much change. That said, the underlying technology is changing, and the competitive landscape provides some new challenges. We want to make sure we

strike the right balance between keeping pace with what's new and what's important in online commerce, and at the same time empower the people who are making their living on eBay.

Q: In particular, some sellers are very unhappy about how eBay recently changed the organization of several product categories, which made it tougher for buyers to browse and thus hurt sales in some categories. Did their complaints hit home?

A: Absolutely. We think books and apparel went really well, helping buyers search for specific products more easily. Music was pretty good, too. As we ventured into pottery and glass, I think we may have moved too fast. There are still a lot of consumers in pottery and glass who like to browse, and that was disrupted somewhat by the category changes. We're going to slow down [those types of changes] until we determine the exact business impact on our sellers.

Q: How do you balance the competing demands of buyers and sellers?

A: It's an art, not a science. We've gotten pretty experienced at it now. We can anticipate the reaction because we ask both buyers and sellers. Then it comes back to: What's the right thing for the marketplace? Sometimes we come down on the side of the sellers, sometimes we come down on the side of the buyers. We really think hard about it.

We rarely make a big change without running a beta, where we run a new site in parallel with the existing one. We never used to do that, because we didn't have the technical capability. We do now.

Q: On eBay's own discussion boards, sellers aren't shy about pointing out what they view as problems. How do you sift through those complaints to determine what's really important?

A: The scale of this user base is so large that part of [managing it] is being able to parse what one ought to do based on the feedback. We have community development teams who know each discussion-board poster.

We think most of our sellers are very happy. But they're like the

silent majority. We do extensive surveys of the community. For example, we surveyed 50,000 people on the changes to My eBay [a customized page for buyers and sellers]. About 80 percent liked it. If we get 80 percent approval, we're good to go.

Q: eBay's international business is growing much faster than in the United States. How does that change the nature of the company?

A: It used to be that the United States was largely the innovation engine. Now, it is the United States and Germany. And Germany has a very significant say in how this platform develops. So I think that as more countries get to that scale, we will include them even more in product-development strategy.

Q: Has the proliferation of eBay around the world changed how people buy and sell?

A: I hear all the time that Germans trade on the Italy site. They may not speak much Italian, but the site is laid out the same way, so they kind of know how to do it. And it's the same with French [going to] the Italian site, and Germans to the U.K. one. In the long run, the way the site works consistently

across geographies is going to be really important to global trade.

Q: The rumor on the floor of eBay Live! is that you might leave eBay before long, possibly for Walt Disney (DIS), where CEO Michael Eisner has been under fire.

A: [Laughs] As far as I know, there isn't a vacancy at Disney. People speculate a lot. But I have to tell you, I have one of the best jobs in Corporate America. It's this unique blend of commerce and community. The community of users is endlessly interesting and endlessly surprising. That's what I love the most.

Questions

1. In what ways does eBay design its IT to control its relationships with buyers and sellers?
2. How does eBay make sure that changes to its control systems over time improve interactions between buyers and sellers?

Source: Robert Hof, "The Constant Challenge at eBay," Reprinted from the June 30, 2004, issue of *BusinessWeek* online by special permission. Copyright © 2004 by the McGraw-Hill Companies, Inc.

BusinessWeek

Case in the News

Vital Signs at Humana

When Michael B. McCallister took over at Humana Inc. four years ago, the Louisville-based health insurer was on the critical list. Its commercial business was bleeding red ink, and it faced the potential loss of government contracts that constituted a third of its revenues. In the ultimate irony,

the health insurer was suffering from a problem all too familiar to its customers: soaring employee health-care costs. After years of double-digit increases, McCallister was facing an expected 19.2 percent surge in his company's health costs in 2001.

That's when the 52-year-old former hospital administrator began his radical surgery. He quickly exited the 15 states where Humana's com-

mercial group was weakest and moved to secure its grip on lucrative government contracts. And to rein in his own spiraling health-care costs, McCallister restructured Humana's health plan to coax 4,800 headquarters workers to manage their own health-care spending before the company's coverage kicked in. In doing so, McCallister hoped to sensitize his own employees to the true costs of medical care—and force

them to be more discriminating in their use of high-cost specialists, emergency rooms, and procedures like CAT scans. He recalls: "I told my employees, 'I'm not going to be your father anymore. I'm going to set the table for you to make your own health decisions.'"

McCallister's triage paid off. Bolstered by a subsequent increase in Medicare reimbursements, he reversed the \$382.4 million loss Humana suffered the year before he became CEO with a healthy \$228 million profit in 2003.

But despite a strong first quarter this year—in which profits rose 117 percent—some investors clearly are betting that McCallister can't sustain his turnaround much longer. That's why McCallister is embarking on his boldest gambit to date: persuading his corporate clients to adopt the same "consumer-driven" health policies Humana successfully deployed three years ago. The move may represent McCallister's best shot at ensuring Humana's independence at a time when larger rivals like Anthem and UnitedHealth Group are gobbling up regional players like Humana. Even if he's successful, those giants may still target Humana—which has one-eighth the member base of UnitedHealth—for

takeover, analysts say.

The theory behind the new medical plans is that the only way to break the spiral of ever-rising health-care costs is to give employees a direct incentive to reduce their expenses. Says McCallister: "We've tried everything else—legislative restrictions, turning doctors into risk-takers—but the one thing we haven't done is turn to the actual users of health care and power them up." Under the plans, workers get a basic level of annual medical coverage—say, \$500 per family member. When those funds are exhausted, workers are subjected to a deductible, perhaps \$3,000 per family. That sounds steep, but it's offset by the fact that employees are no longer paying monthly premiums for their coverage. Once the deductible is met, the employer generally provides full coverage of additional expenses for the year.

Critics worry that to save money, consumers may stint on care—creating bigger health problems, and bigger bills, down the road. McCallister dismisses such concerns, arguing that the biggest savings come from some simple shifts in consumer behavior—from costly specialists to primary-care physicians, and from branded drugs to

cheaper generics. Humana does its part, offering Internet-based tools to help members compare health plans and monitor their expenses.

For all of McCallister's proselytizing, companies have been slow to embrace the new policies. Of the 3 million members in Humana's commercial accounts, just 225,000 have enrolled in SmartSuite. "There's a lot of inertia," McCallister admits. "But we're going through exactly what HMOs went through when they were introduced in the 1980s." McCallister has to hope that his customers see the light. Otherwise, Humana will remain vulnerable to getting swept aside in the rapidly evolving health-care industry.

Questions

1. How did CEO McCallister change Humana's control system to change the behavior of its employees?
2. How did he then try to change the behavior of his customers?

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CHAPTER

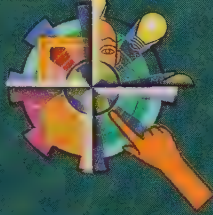
9

Motivation

Learning Objectives

After studying this chapter, you should be able to:

- Explain what motivation is and why managers need to be concerned about it.
- Describe from the perspectives of expectancy theory and equity theory what managers should do to have a highly motivated workforce.
- Explain how goals and needs motivate people and what kinds of goals are especially likely to result in high performance.
- Identify the motivation lessons that managers can learn from operant conditioning theory and social learning theory.
- Explain why and how managers can use pay as a major motivation tool.



Management Snapshot

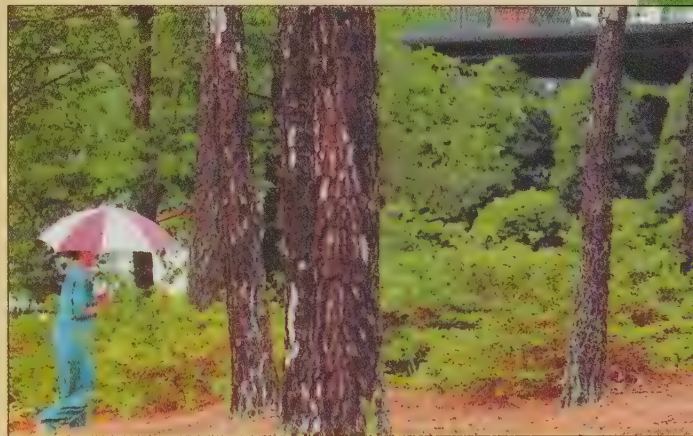
Motivating Employees at the SAS Institute

How can managers sustain high levels of employee motivation over time?

The SAS Institute has ranked in the top 20 of *Fortune* magazine's "100 Best Companies to Work For" ever since the magazine starting compiling these lists in 1998, and 2005 was no exception. In fact, SAS is one of only 22 companies that have made the list every year and is in *Fortune's* Hall of Fame.¹ The SAS Institute is the world's largest privately owned software company, with over 9,000 employees worldwide and approximately \$1.5 billion in sales.² Every indicator suggests that SAS employees are highly motivated and perform well while also working 35-hour weeks. How do managers at SAS do it? In large part, by ensuring that employees are highly motivated and the variety of needs they bring to the workplace are satisfied by doing a good job at SAS.³

Satisfying the need for intrinsically motivating work has also been a key priority at SAS. Managers strive to make sure that each employee is motivated by the work he or she performs, and employees are encouraged to

change jobs to prevent becoming bored with their work (even if the job changes require that SAS provide additional training). Moreover, in contrast to the approach at some of the company's competitors, all new product



An SAS Institute employee makes her way to the dining hall on the 200-acre SAS campus located in Cary, N.C. SAS Institute is known as one of the best companies to work for in the country, offering jogging paths, a gymnasium, and a Montessori preschool on the campus.

development work at SAS is performed in-house, so employees have the opportunity to experience the excitement of developing a new product and seeing it succeed.⁴

The SAS Institute satisfies employees' needs for economic security by paying them fairly and providing them with secure jobs. Employees have their own offices, and the

work environment is rich in pleasant vistas, whether they be artwork on the walls or views of the rolling hills of Cary, North Carolina, at company headquarters. Managers at SAS realize that needs for work-life balance are a top priority for many of their employees and seek to satisfy these needs in a variety of ways, including 35-hour workweeks, on-site day care and medical care, unlimited sick days, and high chairs in the company cafeteria so that employees can dine with their kids. Moreover, employees and their families are encouraged to use the 200 acres that sur-

round company headquarters for family walks and picnics.⁵

James Goodnight, one of SAS's co-founders and its CEO since 1976, is a computer programmer himself and continues to write code. Goodnight and SAS have always strived to satisfy customers with innovative software developed by highly motivated employees who have a good work-life balance.⁶ In fact, an enduring value at SAS is that managers including Goodnight should treat employees the way that the managers would like to be treated themselves.⁷

Overview

Even with the best strategy in place and an appropriate organizational architecture, an organization will be effective only if its members are motivated to perform at a high level. James Goodnight clearly realizes this. One reason why leading is such an important managerial activity is that it entails ensuring that each member of an organization is motivated to perform highly and help the organization achieve its goals. When managers are effective, the outcome of the leading process is a highly motivated workforce. A key challenge for managers of organizations both large and small is to encourage employees to perform at a high level.

In this chapter we describe what motivation is, where it comes from, and why managers need to promote high levels of it for an organization to be effective and achieve its goals. We examine important theories of motivation: expectancy theory, need theories, equity theory, goal-setting theory, and learning theories. Each provides managers with important insights about how to motivate organizational members. The theories are complementary in that each focuses on a somewhat different aspect of motivation. Considering all of the theories together helps managers gain a rich understanding of the many issues and problems involved in encouraging high levels of motivation throughout an organization. Last, we consider the use of pay as a motivation tool. By the end of this chapter, you will understand what it takes to have a highly motivated workforce.

The Nature of Motivation

motivation

Psychological forces that determine the direction of a person's behavior in an organization, a person's level of effort, and a person's level of persistence.

Motivation may be defined as psychological forces that determine the direction of a person's behavior in an organization, a person's level of effort, and a person's level of persistence in the face of obstacles.⁸ The *direction of a person's behavior* refers to the many possible behaviors that a person could engage in. *Effort* refers to how hard people work. *Persistence* refers to whether, when faced with roadblocks and obstacles, people keep trying or give up.

Motivation is central to management because it explains *why* people behave the way they do in organizations⁹. Motivation explains why a waiter is polite or rude and why a kindergarten teacher really tries to get children to enjoy learning or just goes through the motions. It explains why some managers truly put their organizations' best interests first whereas others are more concerned with maximizing their

intrinsically motivated behavior

Behavior that is performed for its own sake.

extrinsically motivated behavior

Behavior that is performed to acquire material or social rewards or to avoid punishment.

outcome Anything a person gets from a job or organization.

salaries and why—more generally—some workers put forth twice as much effort as others.

Motivation can come from *intrinsic* or *extrinsic* sources. **Intrinsically motivated behavior** is behavior that is performed for its own sake; the source of motivation is actually performing the behavior, and motivation comes from doing the work itself. Many managers are intrinsically motivated; they derive a sense of accomplishment and achievement from helping the organization to achieve its goals and gain competitive advantages. Jobs that are interesting and challenging such as those at the SAS Institute are more likely to lead to intrinsic motivation than are jobs that are boring or do not make use of a person's skills and abilities. An elementary school teacher who really enjoys teaching children, a computer programmer who loves solving programming problems, and a commercial photographer who relishes taking creative photographs are all intrinsically motivated. For these individuals, motivation comes from performing their jobs whether it be teaching children, finding bugs in computer programs, or taking pictures.

Extrinsically motivated behavior is behavior that is performed to acquire material or social rewards or to avoid punishment; the source of motivation is the consequences of the behavior, not the behavior itself. A car salesperson who is motivated by receiving a commission on all cars sold, a lawyer who is motivated by the high salary and status that go along with the job, and a factory worker who is motivated by the opportunity to earn a secure income are all extrinsically motivated. Their motivation comes from the consequences they receive as a result of their work behaviors.

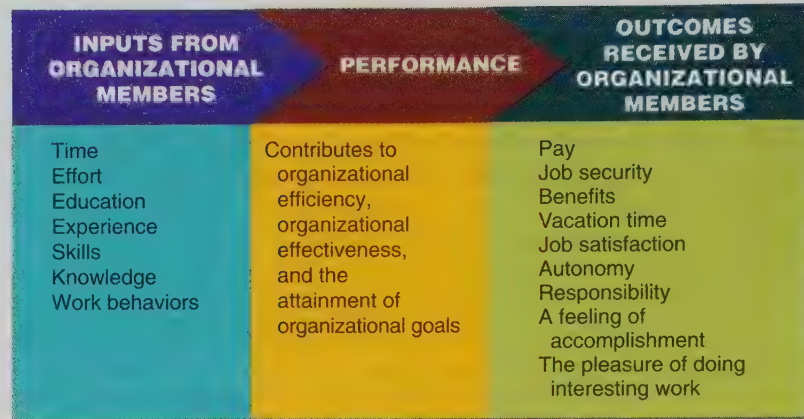
People can be intrinsically motivated, extrinsically motivated, or both intrinsically and extrinsically motivated.¹⁰ A top manager who derives a sense of accomplishment and achievement from managing a large corporation and strives to reach year-end targets to obtain a hefty bonus is both intrinsically and extrinsically motivated. Similarly, a nurse who enjoys helping and taking care of patients and is motivated by having a secure job with good benefits is both intrinsically and extrinsically motivated. Whether workers are intrinsically motivated, extrinsically motivated, or both depends on a wide variety of factors: (1) workers' own personal characteristics (such as their personalities, abilities, values, attitudes, and needs), (2) the nature of their jobs, and (3) the nature of the organization (such as its structure, its culture, its control systems, its human resource management system, and the ways in which rewards such as pay are distributed to employees).

Regardless of whether people are intrinsically or extrinsically motivated, they join and are motivated to work in organizations to obtain certain outcomes. An **outcome** is anything a person gets from a job or organization. Some outcomes, such as autonomy, responsibility, a feeling of accomplishment, and the pleasure of doing interesting or enjoyable work, result in intrinsically motivated behavior. Other outcomes, such as pay, job security, benefits, and vacation time, result in extrinsically motivated behavior.



Jobs that are challenging are more likely to lead to intrinsic motivation because they make use of a person's skills and abilities. For example, when this elementary school teacher uses her teaching skills to explain a difficult concept, she is being intrinsically motivated by her work.

Figure 9.1
The Motivation
Equation



input Anything a person contributes to his or her job or organization.

Organizations hire people to obtain important inputs. An **input** is anything a person contributes to the job or organization, such as time, effort, education, experience, skills, knowledge, and actual work behaviors. Inputs such as these are necessary for an organization to achieve its goals. Managers strive to motivate members of an organization to contribute inputs—through their behavior, effort, and persistence—that help the organization achieve its goals. How do managers do this? They ensure that members of an organization obtain the outcomes they desire when they make valuable contributions to the organization. Managers use outcomes to motivate people to contribute their inputs to the organization. Giving people outcomes when they contribute inputs and perform well aligns the interests of employees with the goals of the organization as a whole because when employees do what is good for the organization, they personally benefit.

expectancy theory

The theory that motivation will be high when workers believe that high levels of effort lead to high performance and high performance leads to the attainment of desired outcomes.

This alignment between employees and organizational goals as a whole can be described by the motivation equation depicted in Figure 9.1. Managers seek to ensure that people are motivated to contribute important inputs to the organization, that these inputs are put to good use or focused in the direction of high performance, and that high performance results in workers' obtaining the outcomes they desire.

Each of the theories of motivation discussed in this chapter focuses on one or more aspects of this equation. Each theory focuses on a different set of issues that managers need to address to have a highly motivated workforce. Together, the theories provide a comprehensive set of guidelines for managers to follow to promote high levels of employee motivation.

Expectancy Theory

Expectancy theory, formulated by Victor H. Vroom in the 1960s, posits that motivation is high when workers believe that high levels of effort lead to high performance and high performance leads to the attainment of desired outcomes.

Expectancy theory is one of the most popular theories of work motivation because it focuses on all three parts of the motivation equation: inputs, performance,

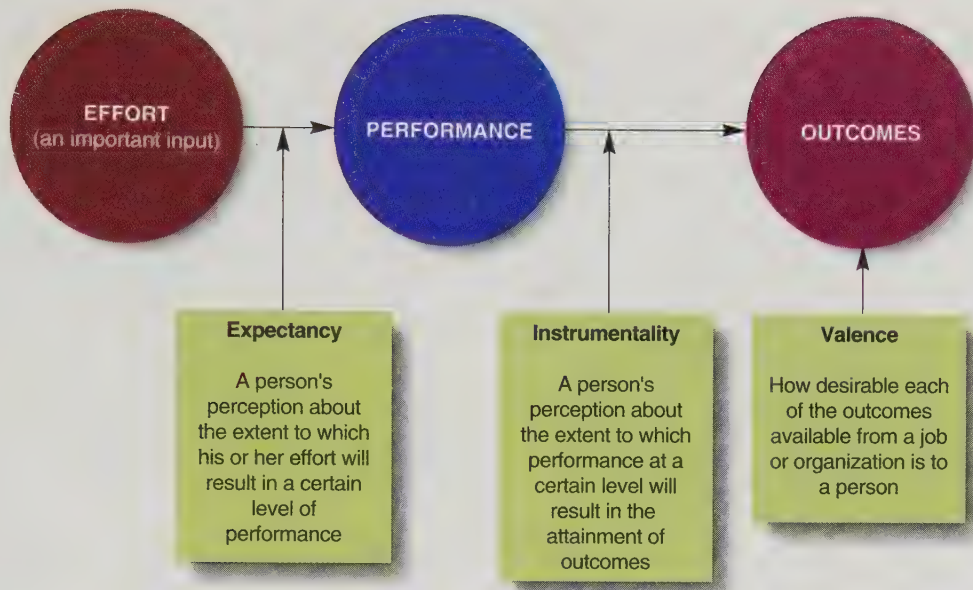


Figure 9.2
Expectancy, Instrumentality, and Valence

and outcomes. Expectancy theory identifies three major factors that determine a person's motivation: expectancy, instrumentality, and valence (see Figure 9.2).¹¹

Expectancy

expectancy In expectancy theory, a perception about the extent to which effort results in a certain level of performance.

Expectancy is a person's perception about the extent to which effort (an input) results in a certain level of performance. A person's level of expectancy determines whether he or she believes that a high level of effort results in a high level of performance. People are motivated to put forth a lot of effort on their jobs only if they think that their effort will pay off in high performance—that is, if they have high expectancy. Think about how motivated you would be to study for a test if you thought that no matter how hard you tried, you would get a D. Think about how motivated a marketing manager would be who thought that no matter how hard he or she worked, there was no way to increase sales of an unpopular product. In these cases, expectancy is low, so overall motivation is also low.

Members of an organization are motivated to put forth a high level of effort only if they think that doing so leads to high performance.¹² In other words, in order for people's motivation to be high, expectancy must be high. Thus, in attempting to influence motivation, managers need to make sure that their subordinates believe that if they do try hard, they can actually succeed. One way managers can boost expectancies is through expressing confidence in their subordinates' capabilities.

In addition to expressing confidence in subordinates, another way for managers to boost subordinates' expectancy levels and motivation is by providing training so that people have all the expertise needed for high performance, as indicated in the following "Information Technology Byte."

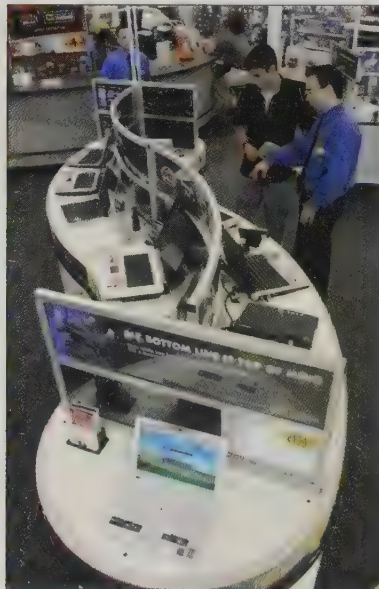
Boosting Expectancy at Best Buy

The Best Buy chain of 629 stores selling electronics, computers, music and movies, and gadgets of all sorts is at an interesting crossroads.¹³ With revenues for fiscal 2004 being over \$24 billion, Best Buy has had another year of double-digit growth in revenues.¹⁴ Best Buy currently has the biggest share of the consumer electronics market in the United States; its key competitors in this market include Wal-Mart, Circuit City, Dell, Target, and RadioShack.¹⁵ However, Wal-Mart is increasing its presence in this market by increasing space in its stores for electronics, and Dell is direct-selling all kinds of electronics ranging from flat-panel TVs to MP3 players.¹⁶

Best Buy is betting its future on its salespeople and their ability to sell customers complete solutions to integrate all their home electronics, ranging from TVs and game players to computers, cameras, and camcorders, into a single system. Given advances in information technology, the advantages of convergence across home electronics are considerable but also complex for many customers.¹⁷ By boosting salespeople's expectancies for being able to sell customers integrated systems, Best Buy hopes to retain its dominant position and distinguish itself from its competitors.

Selling home wireless and integrated systems to customers is complex. Best Buy boosts salespeople's expectancies by providing them with extensive training in on-site meetings and online. Electronic learning terminals in each department not only help salespeople learn how different systems work and can be sold as an integrated package but also enable them to keep up to date with the latest advances in technology and products. Salespeople also receive extensive training in how to determine customers' needs. As CEO Brad Anderson puts it, "You need to really

understand why a customer is in the store and have a detailed knowledge about what products are available to meet that customer's needs. . . . And you need to have fun."¹⁸ Experienced salespeople and managers observe their less experienced co-workers interacting with customers and, once the customer encounter is finished, discuss how it went, what the co-worker did that was effective, and how the co-worker might improve his or her interactions with future customers. When a salesperson successfully completes a significant sale, the store celebrates. Training to boost expectancy is such an integral part of selling at Best Buy that an important criterion for hiring is the extent to which a prospective employee will be "teachable."¹⁹ All in all, the high expectancies salespeople at Best Buy have for selling integrated systems and solutions to customers may help Best Buy stay ahead of competitors like Wal-Mart, known for low prices but unlikely to be able to match Best Buy in terms of responsiveness to customers.²⁰



Best Buy employees go through extensive training to help them with the complex task of selling home wireless and integrated systems.

instrumentality In expectancy theory, a perception about the extent to which performance results in the attainment of outcomes.

Instrumentality

Expectancy captures a person's perceptions about the relationship between effort and performance. **Instrumentality**, the second major concept in expectancy theory, is a person's perception about the extent to which performance at a certain level results in the attainment of outcomes (see Figure 9.2). According to expectancy theory, employees are motivated to perform at a high level only if they think that high performance will lead to (or is *instrumental* for attaining) outcomes such as pay, job security, interesting job assignments, bonuses, or a feeling of accomplishment. In other words, instrumentalities must be high for motivation to be high—people must perceive that because of their high performance they will receive outcomes.²¹

Managers promote high levels of instrumentality when they clearly link performance to desired outcomes. In addition, managers must clearly communicate this linkage to subordinates. By making sure that outcomes available in an organization are distributed to organizational members on the basis of their performance, managers promote high instrumentality and motivation. When outcomes are linked to performance in this way, high performers receive more outcomes than low performers.

An example of high instrumentality contributing to high motivation can be found in the Cambodian immigrants who own, manage, and work in more than 80 percent of the doughnut shops in California.²² These immigrants see high performance as leading to many important outcomes, such as income, a comfortable existence, family security, and the autonomy provided by working in a small business. Their high instrumentality contributes to their high motivation to succeed.

Valence

Although all members of an organization must have high expectancies and instrumentalities, expectancy theory acknowledges that people differ in their preferences for outcomes. For many people, pay is the most important outcome of working. For others, a feeling of accomplishment or enjoying one's work is more important than pay. The term **valence** refers to how desirable each of the outcomes available from a job or organization is to a person. To motivate organizational members, managers need to determine which outcomes have high valence for them—are highly desired—and make sure that those outcomes are provided when members perform at a high level.

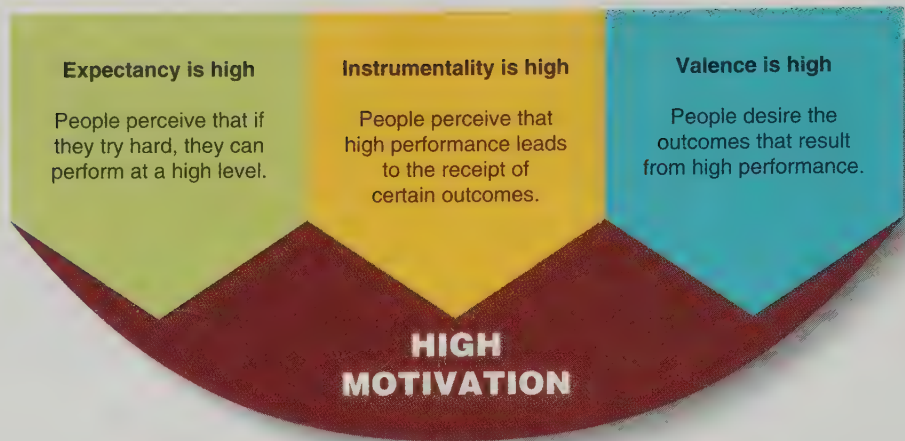
valence In expectancy theory, how desirable each of the outcomes available from a job or organization is to a person.

Bringing it all together

According to expectancy theory, high motivation results from high levels of expectancy, instrumentality, and valence (see Figure 9.3). If any one of these factors is low, motivation is likely to be low. No matter how tightly desired outcomes are linked to performance, if a person thinks it is practically impossible to perform at a high level, then motivation to perform at a high level is exceedingly low. Similarly, if a person does not think that outcomes are linked to high performance, or if a person does not desire the outcomes that are linked to high performance, then motivation to perform at a high level is low.

A key challenge for managers is encouraging high levels of motivation when trying to expand into new markets, especially markets in which an organization might

Figure 9.3
Expectancy
Theory



have previously failed. As indicated in the following “Focus on Diversity,” maintaining high levels of expectancy, instrumentality, and valence and learning from past failures are essential.



Focus on Diversity

Nike's Efforts to Appeal to Diverse Customers

Nike had some failures in the 1980s and 1990s trying to make inroads into new markets. Bowling shoes that left bowlers sliding down bowling alleys on the heels of bowling balls, a commercial for women's apparel that turned women off rather than on to Nike, and a golf shoe that was so uncomfortable employees nicknamed it “air-blister” were among Nike's missteps in trying to appeal to diverse customers in new markets.²³ Fast-forward to 2004, and Nike is once again trying to win over diverse customers in new markets. But this time around, managers have learned from their mistakes and are taking a new approach.²⁴

A key element of Nike's new approach is motivating employees to develop products in nontraditional markets (for Nike) in ways that will lead to high expectancy and instrumentality as well as to products that diverse customers will want to buy. Nike is a huge brand, embraced both by athletes playing team sports and by consumers young and old looking for athletic apparel and gear.²⁵ However, many a skateboarder would loathe having the Nike *swoosh* adorning her or his shoes or clothes. Skateboarders have their own subculture and brands;²⁶ as a poster in a Skatework's store in Redmond, California, reads, “Don't do it!”²⁷

How can employees be motivated to enter this challenging market and woo diverse customers who pride themselves on being hip and unconventional? Essentially, by working in a small “company,” knowing the skateboarding subculture, and taking the time to develop products that they are confident will appeal to skateboarders. Nike Skate, headed by vice president Sandy Bodecker, a ski-racing coach, is an autonomous unit that began with 11 skateboarding employees. They took their time to develop products that would appeal to skateboarders, such as URL, E-Cue, Dunk SB, and Air Angus shoes.²⁸ And they



Nike Skate, an autonomous unit of Nike, which is taking aim at the skateboarding market, will have to win over a skateboarding culture whose motto is "Don't do it!"

also took pains to win over owners of skate shops who were initially reluctant to carry Nike merchandise out of fear that they would ultimately lose some of their customers when discount stores started selling the same Nike merchandise at lower prices. Offering skate shops exclusive rights to stock Nike's skate products helped to quell such fears.²⁹

Nike Skate employees are immersed in the skateboarding culture, listening to music and paging through skateboarding magazines on the job. Managing the new product development process in this manner has helped managers and employees alike have high expectancy that they will be able to develop prod-

ucts that appeal to skateboarders, these products will be instrumental for the growth and revenues of the unit, and the products will appeal to customers. The skateboarding industry takes in about \$1.4 billion in revenues annually. While Nike Skate's current revenues of about \$25 million are just a fraction of the industry total, employees and managers alike are confident that their current approach to winning skateboarding customers will pay off and make Nike popular in this diverse segment of the sporting world.³⁰

Need Theories

need A requirement or necessity for survival and well-being.

need theories

Theories of motivation that focus on what needs people are trying to satisfy at work and what outcomes will satisfy those needs.


A **need** is a requirement or necessity for survival and well-being. The basic premise of **need theories** is that people are motivated to obtain outcomes at work that will satisfy their needs. Need theory complements expectancy theory by exploring in depth which outcomes motivate people to perform at a high level. Need theories suggest that to motivate a person to contribute valuable inputs to a job and perform at a high level, a manager must determine what needs the person is trying to satisfy at work and ensure that the person receives outcomes that help to satisfy those needs when the person performs at a high level and helps the organization achieve its goals.

There are several need theories. Here we discuss Abraham Maslow's hierarchy of needs, Frederick Herzberg's motivator-hygiene theory, and David McClelland's needs for achievement, affiliation, and power. These theories describe needs that people try to satisfy at work. In doing so, they provide managers with insights about what outcomes motivate members of an organization to perform at a high level and contribute inputs to help the organization achieve its goals.

Maslow's hierarchy of needs

Psychologist Abraham Maslow proposed that all people seek to satisfy five basic kinds of needs: physiological needs, safety needs, belongingness needs, esteem needs, and self-actualization needs (see Table 9.1).³¹ He suggested that these

Table 9.1
Maslow's Hierarchy of Needs

	Needs	Description	Examples of How Managers Can Help People Satisfy These Needs at Work
Highest-level needs 	Self-actualization needs	The needs to realize one's full potential as a human being	By giving people the opportunity to use their skills and abilities to the fullest extent possible
	Esteem needs	The needs to feel good about oneself and one's capabilities, to be respected by others, and to receive recognition and appreciation	By granting promotions and recognizing accomplishments
	Belongingness needs	Needs for social interaction, friendship, affection, and love	By promoting good interpersonal relations and organizing social functions such as company picnics and holiday parties
	Safety needs	Needs for security, stability, and a safe environment	By providing job security, adequate medical benefits, and safe working conditions
Lowest-level needs (most basic or compelling)	Physiological needs	Basic needs for things such as food, water, and shelter that must be met in order for a person to survive	By providing a level of pay that enables a person to buy food and clothing and have adequate housing
The lowest level of unsatisfied needs motivates behavior; once this level of needs is satisfied, a person tries to satisfy the needs at the next level.			

Maslow's hierarchy of needs

An arrangement of five basic needs that, according to Maslow, motivate behavior. Maslow proposed that the lowest level of unmet needs is the prime motivator and that only one level of needs is motivational at a time.

needs constitute a **hierarchy of needs**, with the most basic or compelling needs—physiological and safety needs—at the bottom. Maslow argued that these lowest-level needs must be met before a person strives to satisfy needs higher up in the hierarchy, such as self-esteem needs. Once a need is satisfied, Maslow proposed, it ceases to operate as a source of motivation. The lowest level of unmet needs in the hierarchy is the prime motivator of behavior; if and when this level is satisfied, needs at the next-highest level in the hierarchy motivate behavior.

Although this theory identifies needs that are likely to be important sources of motivation for many people, research does not support Maslow's contention that there is a need hierarchy or his notion that only one level of needs is motivational at a time.³² Nevertheless, a key conclusion can be drawn from Maslow's theory: People try to satisfy different needs at work. To have a motivated workforce, managers must determine which needs employees are trying to satisfy in organizations and then make sure that individuals receive outcomes that satisfy their needs when they perform at a high level and contribute to organizational effectiveness. By doing this, managers align the interests of individual members with the interests of the organization as a whole. By doing what is good for the organization (that is, performing at a high level), employees receive outcomes that satisfy their needs.

In our increasingly global economy, managers must realize that citizens of different countries might differ in the needs they seek to satisfy through work.³³ Some

research suggests, for example, that people in Greece and Japan are especially motivated by safety needs and that people in Sweden, Norway, and Denmark are motivated by belongingness needs.³⁴ In less developed countries with low standards of living, physiological and safety needs are likely to be the prime motivators of behavior. As countries become wealthier and have higher standards of living, needs related to personal growth and accomplishment (such as esteem and self-actualization) become important as motivators of behavior.

Herzberg's motivator-hygiene theory

Adopting an approach different from Maslow's, Frederick Herzberg focuses on two factors: (1) outcomes that can lead to high levels of motivation and job satisfaction and (2) outcomes that can prevent people from being dissatisfied. According to Herzberg's **motivator-hygiene theory**, people have two sets of needs or requirements: **motivator needs** and **hygiene needs**.³⁵ Motivator needs are related to the nature of the work itself and how challenging it is. Outcomes, such as **interesting work**, autonomy, responsibility, being able to grow and develop on the job, and a **sense of accomplishment and achievement**, help to satisfy **motivator needs**. To have a highly motivated and satisfied workforce, Herzberg suggested, managers should take steps to ensure that employees' motivator needs are being met.

Hygiene needs are related to the physical and psychological context in which the work is performed. **Hygiene needs are satisfied by outcomes such as pleasant and comfortable working conditions, pay, job security, good relationships with co-workers, and effective supervision.** According to Herzberg, when hygiene needs are not met, **workers are dissatisfied**, and when hygiene needs are met, **workers are not dissatisfied**. Satisfying hygiene needs, however, does not result in high levels of motivation or even high levels of job satisfaction. For motivation and job satisfaction to be high, motivator needs must be met.

Many research studies have tested Herzberg's propositions, and, by and large, the theory fails to receive support.³⁶ Nevertheless, Herzberg's formulations have contributed to our understanding of motivation in at least two ways. First, Herzberg helped to focus researchers' and managers' attention on the important distinction between intrinsic motivation (related to motivator needs) and extrinsic motivation (related to hygiene needs), covered earlier in the chapter. Second, his theory prompted researchers and managers to study how jobs could be designed or redesigned so that they are intrinsically motivating.

McClelland's needs for achievement, affiliation, and power

Psychologist David McClelland has extensively researched the needs for achievement, affiliation, and power.³⁷ The **need for achievement** is the extent to which an individual has a strong desire to perform challenging tasks well and to meet personal standards for excellence. People with a high need for achievement often set clear goals for themselves and like to receive performance feedback. The **need for affiliation** is the extent to which an individual is concerned about establishing and maintaining good interpersonal relations, being liked, and having the people around him or her get along with each other. The **need for power** is the extent to which an individual desires to control or influence others.³⁸

Herzberg's motivator-hygiene theory

A need theory that distinguishes between motivator needs (related to the nature of the work itself) and hygiene needs (related to the physical and psychological context in which the work is performed) and proposes that motivator needs must be met for motivation and job satisfaction to be high.

need for achievement The extent to which an individual has a strong desire to perform challenging tasks well and to meet personal standards for excellence.

need for affiliation The extent to which an individual is concerned about establishing and maintaining good interpersonal relations, being liked, and having the people around him or her get along with each other.

need for power The extent to which an individual desires to control or influence others.

While each of these needs is present in each of us to some degree, their importance in the workplace depends upon the position one occupies. For example, research suggests that high needs for achievement and for power are assets for first-line and middle managers and that a high need for power is especially important for upper managers.³⁹ One study found that U.S. presidents with a relatively high need for power tended to be especially effective during their terms of office.⁴⁰ A high need for affiliation may not always be desirable in managers and other leaders because it might lead them to try too hard to be liked by others (including subordinates) rather than doing all they can to ensure that performance is as high as it can and should be. Although most research on these needs has been done in the United States, some studies suggest that the findings may be applicable to people in other countries as well, such as India and New Zealand.⁴¹

Other needs

Clearly more needs motivate workers than the needs described by the above three theories. For example, more and more workers are feeling the need for work-life balance and time to take care of their loved ones while simultaneously being highly motivated at work. Interestingly enough, recent research suggests that being exposed to nature (even just being able to see some trees from your office window) has many salutary effects and a lack of such exposure can actually impair well-being and performance.⁴² Thus, having some time during the day when one can at least see nature may be another important need.

Equity Theory

equity theory A theory of motivation that focuses on people's perceptions of the fairness of their work outcomes relative to their work inputs.

Equity theory is a theory of motivation that concentrates on people's perceptions of the fairness of their work *outcomes* relative to, or in proportion to, their work *inputs*. Equity theory complements expectancy and need theories by focusing on how people perceive the relationship between the outcomes they receive from their jobs and organizations and the inputs they contribute. Equity theory was formulated in the 1960s by J. Stacy Adams, who stressed that what is important in determining motivation is the *relative* rather than the *absolute* levels of outcomes a person receives and inputs a person contributes. Specifically, motivation is influenced by the comparison of one's own outcome-input ratio with the outcome-input ratio of a referent.⁴³ The *referent* could be another person or a group of people who are perceived to be similar to oneself; the referent also could be oneself in a previous job or one's expectations about what outcome-input ratios should be. In a comparison of one's own outcome-input ratio to a referent's outcome-input ratio, one's *perceptions* of outcomes and inputs (not any objective indicator of them) are key.

Equity

equity The justice, impartiality, and fairness to which all organizational members are entitled.

Equity exists when a person perceives his or her own outcome-input ratio to be equal to a referent's outcome-input ratio. Under conditions of equity (see Table 9.2), if a referent receives more outcomes than you receive, the referent contributes proportionally more inputs to the organization, so his or her outcome-input ratio still equals your outcome-input ratio. Maria Sanchez and Claudia King, for example, both work in a shoe store in a large mall. Sanchez is paid more per hour than King but also contributes more inputs, including being responsible for some of the store's

Table 9.2
Equity Theory

Condition	Person		Referent	Example
Equity	$\frac{\text{Outcomes}}{\text{Inputs}}$	=	$\frac{\text{Outcomes}}{\text{Inputs}}$	An engineer perceives that he contributes more inputs (time and effort) and receives proportionally more outcomes (a higher salary and choice job assignments) than his referent.
Underpayment inequity	$\frac{\text{Outcomes}}{\text{Inputs}}$	< (less than)	$\frac{\text{Outcomes}}{\text{Inputs}}$	An engineer perceives that he contributes more inputs but receives the same outcomes as his referent.
Overpayment inequity	$\frac{\text{Outcomes}}{\text{Inputs}}$	> (greater than)	$\frac{\text{Outcomes}}{\text{Inputs}}$	An engineer perceives that he contributes the same inputs but receives more outcomes than his referent.

bookkeeping, closing the store, and periodically depositing cash in the bank. When King compares her outcome-input ratio to Sanchez's (her referent's), she perceives the ratios to be equitable because Sanchez's higher level of pay (an outcome) is proportional to her higher level of inputs (bookkeeping, closing the store, and going to the bank).

Similarly, under conditions of equity, if you receive more outcomes than a referent, then your inputs are perceived to be proportionally higher. Continuing with our example, when Sanchez compares her outcome-input ratio to King's (her referent's) outcome-input ratio, she perceives them to be equitable because her higher level of pay is proportional to her higher level of inputs.

When equity exists, people are motivated to continue contributing their current levels of inputs to their organizations to receive their current levels of outcomes. If people wish to increase their outcomes under conditions of equity, they are motivated to increase their inputs.

Inequity

inequity Lack of fairness.

underpayment inequity The inequity that exists when a person perceives that his or her own outcome-input ratio is less than the ratio of a referent.

overpayment inequity The inequity that exists when a person perceives that his or her own outcome-input ratio is greater than the ratio of a referent.

Inequity, lack of fairness, exists when a person's outcome-input ratio is not perceived to be equal to a referent's. Inequity creates pressure or tension inside people and motivates them to restore equity by bringing the two ratios back into balance.

There are two types of inequity: underpayment inequity and overpayment inequity (see Table 9.2). **Underpayment inequity** exists when a person's own outcome-input ratio is perceived to be *less* than that of a referent. In comparing yourself to a referent, you think that you are *not* receiving the outcomes you should be, given your inputs. **Overpayment inequity** exists when a person perceives that his or her own outcome-input ratio is *greater* than that of a referent. In comparing yourself to a referent, you think that you are receiving *more* outcomes than you should be, given your inputs.

Ways to restore equity

According to equity theory, both underpayment inequity and overpayment inequity create tension that motivates most people to restore equity by bringing the ratios

back into balance.⁴⁴ When people experience *underpayment* inequity, they may be motivated to lower their inputs by reducing their working hours, putting forth less effort on the job, or being absent or they may be motivated to increase their outcomes by asking for a raise or a promotion. Susan Richie, a financial analyst at a large corporation, noticed that she was working longer hours and getting more work accomplished than a co-worker who had the same position, yet they both received the exact same pay and other outcomes. To restore equity, Richie decided to stop coming in early and staying late. Alternatively, she could have tried to restore equity by trying to increase her outcomes, say, by asking her boss for a raise.

When people experience underpayment inequity and other means of equity restoration fail, they can change their perceptions of their own or the referents' inputs or outcomes. For example, they may realize that their referent is really working on more difficult projects than they are or that they really take more time off from work than their referent does. Alternatively, if people who feel that they are underpaid have other employment options, they may leave the organization. As an example, John Steinberg, an assistant principal in a high school, experienced underpayment inequity when he realized that all of the other assistant principals of high schools in his school district had received promotions to the position of principal even though they had been in their jobs for a shorter time than he had been. Steinberg's performance had always been appraised as being high, so after his repeated requests for a promotion went unheeded, he found a job as a principal in a different school district.

When people experience *overpayment* inequity, they may try to restore equity by changing their perceptions of their own or their referents' inputs or outcomes. Equity can be restored when people realize that they are contributing more inputs than they originally thought. Equity also can be restored by perceiving the referent's inputs to be lower or the referent's outcomes to be higher than one originally thought. When equity is restored in this way, actual inputs and outcomes are unchanged and the person being overpaid takes no real action. What is changed is how people think about or view their or the referent's inputs and outcomes. For instance, Mary McMann experienced overpayment inequity when she realized that she was being paid \$2 an hour more than a co-worker who had the same job as she did in a record store and who contributed the same amount of inputs. McMann restored equity by changing her perceptions of her inputs. She realized that she worked harder than her co-worker and solved more problems that came up in the store.

Experiencing either overpayment or underpayment inequity, you might decide that your referent is not appropriate because, for example, the referent is too different from yourself. Choosing a more appropriate referent may bring the ratios back into balance. Angela Martinez, a middle manager in the engineering department of a chemical company, experienced overpayment inequity when she realized that she was being paid quite a bit more than her friend who was a middle manager in the marketing department of the same company. After thinking about the discrepancy for a while, Martinez decided that engineering and marketing were so different that she should not be comparing her job to her friend's job even though they were both middle managers. Martinez restored equity by changing her referent; she picked a fellow middle manager in the engineering department as a new referent.

Motivation is highest when as many people as possible in an organization perceive that they are being treated equitably—their outcomes and inputs are in



Whether or not this employee receives pay for overtime depends on her status as an exempt or nonexempt employee.

balance. Top contributors and performers are motivated to continue contributing a high level of inputs because they are receiving the outcomes they deserve. Mediocre contributors and performers realize that if they want to increase their outcomes, they have to increase their inputs.

The dot-com boom, subsequent bust, and a recession, along with increased global competition, have resulted in some workers' putting in longer and longer working hours (i.e., increasing their inputs) without any kind of increase in their outcomes. For those whose referents are not experiencing a similar change, perceptions of inequity are likely. According to Jill Andresky Fraser, author of *White Collar Sweatshop*, over 25 million U.S. workers work more than 49 hours per week in the office, almost 11 million work more than 60 hours per week in the office, and many also put in additional work

hours at home. Moreover, advances in information technology, such as email and cell phones, have resulted in work intruding on home time, vacation time, and even special occasions.⁴⁵

Goal-Setting Theory

Goal-setting theory focuses on motivating workers to contribute their inputs to their jobs and organizations; in this way it is similar to expectancy theory and equity theory. But goal-setting theory takes this focus a step further

by considering as well how managers can ensure that organizational members focus their inputs in the direction of high performance and the achievement of organizational goals.

Ed Locke and Gary Latham, the leading researchers on goal-setting theory, suggest that the goals that organizational members strive to attain are prime determinants of their motivation and subsequent performance. A *goal* is what a person is trying to accomplish through his or her efforts and behaviors.⁴⁶ Just as you may have a goal to get a good grade in this course, so do members of an organization have goals that they strive to meet. For example, salespeople at Neiman Marcus strive to meet sales goals, while top managers pursue market share and profitability goals.

Goal-setting theory suggests that to stimulate high motivation and performance, goals must be *specific* and *difficult*.⁴⁷ Specific goals are often quantitative—a salesperson's goal to sell \$200 worth of merchandise per day, a scientist's goal to finish a project in one year, a CEO's goal to reduce debt by 40 percent and increase revenues by 20 percent, a restaurant manager's goal to serve 150 customers per evening. In contrast to specific goals, vague goals such as "doing your best" or "selling as much as you can" do not have much motivational impact.

Difficult goals are hard but not impossible to attain. In contrast to difficult goals, easy goals are those that practically everyone can attain, and moderate goals are

goal-setting theory

A theory that focuses on identifying the types of goals that are most effective in producing high levels of motivation and performance and explaining why goals have these effects.

goals that about one-half of the people can attain. Both easy and moderate goals have less motivational power than difficult goals.

Regardless of whether specific, difficult goals are set by managers, workers, or teams of managers and workers, they lead to high levels of motivation and performance. When managers set goals for their subordinates, their subordinates must accept the goals or agree to work toward them; also, they should be committed to them or really want to attain them. Some managers find having subordinates participate in the actual setting of goals boosts their acceptance of and commitment to the goals. In addition, organizational members need to receive *feedback* about how they are doing; feedback can often be provided by the performance appraisal and feedback component of an organization's human resource management system (see Chapter 12).

Specific, difficult goals affect motivation in two ways. First, they motivate people to contribute more inputs to their jobs. Specific, difficult goals cause people to put forth high levels of effort, for example. Just as you would study harder if you were trying to get an A in a course instead of a C, so too will a salesperson work harder to reach a \$200 sales goal instead of a \$100 goal. Specific, difficult goals also cause people to be more persistent than easy, moderate, or vague goals when they run into difficulties. Salespeople who are told to sell as much as possible might stop trying on a slow day, whereas having a specific, difficult goal to reach causes them to keep trying.

A second way in which specific, difficult goals affect motivation is by helping people focus their inputs in the right direction. These goals let people know what they should be focusing their attention on, be it increasing the quality of customer service or sales or lowering new product development times. The fact that the goals are specific and difficult also frequently causes people to develop *action plans* for reaching them.⁴⁸ Action plans can include the strategies to attain the goals and timetables or schedules for the completion of different activities crucial to goal attainment. Like the goals themselves, action plans also help ensure that efforts are focused in the right direction and that people do not get sidetracked along the way.

When top managers take over troubled companies, it is often important for them to set specific, difficult goals for themselves and their employees in order to focus and direct their own efforts and the efforts of the company, as indicated in the following "Focus on Diversity."



Focus on Diversity

Dick Parsons Gets Time Warner Back on Track

When Richard "Dick" Parsons took over as CEO of the troubled AOL Time Warner (now called Time Warner), he was on the receiving end of numerous complaints from disgruntled shareholders. The stockholders were dissatisfied with the performance of the company, the quality of customer service at AOL, and even the company's new headquarters, which was under construction at New York City's Columbus Circle.⁴⁹ Parsons diplomatically responded to these complaints in his first meeting with shareholders.⁵⁰

Parsons is leading a successful turnaround of Time Warner, and his effectiveness as CEO, and now also as chairman of the board,⁵¹ is at least partially attributable to the specific, difficult goals he sets for himself and to his practice of



So far Time Warner's performance under the leadership of CEO Dick Parsons has earned the thumbs up sign from some tough critics.

holding employees accountable for achieving their goals. Parsons identified key goals that he needed to pursue: Reduce debt levels, increase performance, shore up AOL, and motivate employees to want to achieve their goals. From day 1, his focus was on goals that could be accomplished in the near term (say, 6 to 12 months) rather than the lofty kinds of goals that had gotten the company into trouble.⁵² And he worked to stay committed to these goals until they were accomplished. Prior to his assuming the top job, Time Warner was becoming known for "shifting gears every 30 days," according to Don Logan, who Parsons appointed as chairman of media and communication.⁵³

In less than two years, Parsons has met many of his goals, and employees at Time Warner are meeting their goals. The stock price has risen considerably, and the company's debt has been reduced by \$10 billion. Performance of divisions such as cable TV and Hollywood studios is up, and cooperation has replaced the power struggles and infighting that used to take place among top managers and feed down to employees.⁵⁴ And employee morale and motivation have improved as goals are being met and company performance is being enhanced. As Parsons indicates, "People have a sense we're making progress."⁵⁵

In 2004, Parsons was named as one of the most powerful African-American executives by *Fortune* magazine.⁵⁶ It was Parsons's careful approach to setting Time Warner back on track with specific and difficult goals that has led the company to once again be making inroads in offering new technologies such as Internet protocol telephony.⁵⁷ Parsons also realizes the importance of intrinsic motivation. As he told the 2004 graduating class at New York University in his commencement address, "When you love what you do, work becomes something to be enjoyed rather than endured . . . seek to serve some good greater than your own."⁵⁸

Although specific, difficult goals have been found to increase motivation and performance in a wide variety of jobs and organizations both in the United States and abroad, recent research suggests that they may detract from performance under certain conditions. When people are performing complicated and very challenging tasks that require a considerable amount of learning, specific, difficult goals may actually impair performance.⁵⁹ All of a person's attention needs to be focused on learning complicated and difficult tasks. Striving to reach a specific, difficult goal may detract from performance on complex tasks because some of a person's attention is directed away from learning about the task and toward trying to figure out how to achieve the goal. Once a person has learned the task and it no longer seems complicated or difficult, then the assignment of specific, difficult goals is likely to have its usual effects. Additionally, for work that is very creative and uncertain, specific, difficult goals may be detrimental.

Learning Theories

learning theories

Theories that focus on increasing employee motivation and performance by linking the outcomes that employees receive to the performance of desired behaviors and the attainment of goals.

learning A relatively permanent change in knowledge or behavior that results from practice or experience.

operant conditioning theory

The theory that people learn to perform behaviors that lead to desired consequences and learn not to perform behaviors that lead to undesired consequences.

positive reinforcement

Giving people outcomes they desire when they perform organizationally functional behaviors.

negative reinforcement

Eliminating or removing undesired outcomes when people perform organizationally functional behaviors.

The basic premise of **learning theories** as applied to organizations is that managers can increase employee motivation and performance by the ways they link the outcomes that employees receive to the performance of

desired behaviors in an organization and the attainment of goals. Thus, learning theory focuses on the linkage between performance and outcomes in the motivation equation (see Figure 9.1).

Learning can be defined as a relatively permanent change in a person's knowledge or behavior that results from practice or experience.⁶⁰ Learning takes place in organizations when people learn to perform certain behaviors to receive certain outcomes. For example, a person learns to perform at a higher level than in the past or to come to work earlier because he or she is motivated to obtain the outcomes that result from these behaviors, such as a pay raise or praise from a supervisor. Of the different learning theories, operant conditioning theory and social learning theory provide the most guidance to managers in their efforts to have a highly motivated workforce.

Operant conditioning theory

According to **operant conditioning theory**, developed by psychologist B. F. Skinner, people learn to perform behaviors that lead to desired consequences and learn not to perform behaviors that lead to undesired consequences.⁶¹ Translated into motivation terms, Skinner's theory means that people will be motivated to perform at a high level and attain their work goals to the extent that high performance and goal attainment allow them to obtain outcomes they desire. Similarly, people avoid performing behaviors that lead to outcomes they do not desire. By linking the performance of *specific behaviors* to the attainment of *specific outcomes*, managers can motivate organizational members to perform in ways that help an organization achieve its goals.

Operant conditioning theory provides four tools that managers can use to motivate high performance and prevent workers from engaging in absenteeism and other behaviors that detract from organizational effectiveness. These tools are positive reinforcement, negative reinforcement, extinction, and punishment.⁶²

POSITIVE REINFORCEMENT **Positive reinforcement** gives people outcomes they desire when they perform organizationally functional behaviors. These desired outcomes, called *positive reinforcers*, include any outcomes that a person desires, such as pay, praise, or a promotion. Organizationally functional behaviors are behaviors that contribute to organizational effectiveness; they can include producing high-quality goods and services, providing high-quality customer service, and meeting deadlines. By linking positive reinforcers to the performance of functional behaviors, managers motivate people to perform the desired behaviors.

NEGATIVE REINFORCEMENT **Negative reinforcement** also can encourage members of an organization to perform desired or organizationally functional behaviors. Managers using negative reinforcement actually eliminate or remove undesired outcomes once the functional behavior is performed. These undesired outcomes, called *negative reinforcers*, can range from a manager's constant nagging or criticism to unpleasant assignments to the ever-present threat of losing one's job.

When negative reinforcement is used, people are motivated to perform behaviors because they want to stop receiving or avoid undesired outcomes. Managers who try to encourage salespeople to sell more by threatening them with being fired are using negative reinforcement. In this case, the negative reinforcer is the threat of job loss, which is removed once the functional behavior is performed.

Whenever possible, managers should try to use positive reinforcement. Negative reinforcement can create a very unpleasant work environment and even a negative culture in an organization. No one likes to be nagged, threatened, or exposed to other kinds of negative outcomes. The use of negative reinforcement sometimes causes subordinates to resent managers and try to get back at them.

IDENTIFYING THE RIGHT BEHAVIORS FOR REINFORCEMENT Even managers who use positive reinforcement (and refrain from using negative reinforcement) can get into trouble if they are not careful to identify the right behaviors to reinforce—behaviors that are truly functional for the organization. Doing this is not always as straightforward as it might seem. First, it is crucial for managers to choose behaviors over which subordinates have control; in other words, subordinates must have the freedom and opportunity to perform the behaviors that are being reinforced. Second, it is crucial that these behaviors contribute to organizational effectiveness.

EXTINCTION Sometimes members of an organization are motivated to perform behaviors that actually detract from organizational effectiveness. According to operant conditioning theory, all behavior is controlled or determined by its consequences; one way for managers to curtail the performance of dysfunctional behaviors is to eliminate whatever is reinforcing the behaviors. This process is called

extinction.

extinction Curtailing the performance of dysfunctional behaviors by eliminating whatever is reinforcing them.

Suppose a manager has a subordinate who frequently stops by his office to chat—sometimes about work-related matters but at other times about various topics ranging from politics to last night's football game. The manager and the subordinate share certain interests and views, so these conversations can get quite involved, and both seem to enjoy them. The manager, however, realizes that these frequent and sometimes lengthy conversations are actually causing him to stay at work later in the evenings to make up for the time he loses during the day. The manager also realizes that he is actually reinforcing his subordinate's behavior by acting interested in the topics the subordinate brings up and responding at length to them. To extinguish this behavior, the manager stops acting interested in these non-work-related conversations and keeps his responses polite and friendly but brief. No longer being reinforced with a pleasurable conversation, the subordinate eventually ceases to be motivated to interrupt the manager during working hours to discuss non-work-related issues.

PUNISHMENT Sometimes managers cannot rely on extinction to eliminate dysfunctional behaviors because they do not have control over whatever is reinforcing the behavior or because they cannot afford the time needed for extinction to work. When employees are performing dangerous behaviors or behaviors that are illegal or unethical, the behavior needs to be eliminated immediately. Sexual harassment, for example, is an organizationally dysfunctional behavior that cannot be tolerated. In such cases managers often rely on **punishment**, administering an undesired or negative consequence to subordinates when they perform the dysfunctional behavior. Punishments used by organizations range from verbal

punishment Administering an undesired or negative consequence when dysfunctional behavior occurs.

reprimands to pay cuts, temporary suspensions, demotions, and firings. Punishment, however, can have some unintended side effects—resentment, loss of self-respect, a desire for retaliation—and should be used only when necessary.

To avoid the unintended side effects of punishment, managers should keep in mind these guidelines:

- Downplay the emotional element involved in punishment. Make it clear that you are punishing a person's performance of a dysfunctional behavior, not the person himself or herself.
- Try to punish dysfunctional behaviors as soon after they occur as possible, and make sure the negative consequence is a source of punishment for the individuals involved. Be certain that organizational members know exactly why they are being punished.
- Try to avoid punishing someone in front of others, for this can hurt a person's self-respect and lower esteem in the eyes of co-workers as well as make co-workers feel uncomfortable.⁶³ Even so, making organizational members aware that an individual who has committed a serious infraction has been punished can sometimes be effective in preventing future infractions and teaching all members of the organization that certain behaviors are unacceptable. For example, when organizational members are informed that a manager who has sexually harassed subordinates has been punished, they learn or are reminded of the fact that sexual harassment is not tolerated in the organization.

Managers and students alike often confuse negative reinforcement and punishment. To avoid such confusion, keep in mind the two major differences between them. First, negative reinforcement is used to promote the performance of functional behaviors in organizations; punishment is used to stop the performance of dysfunctional behaviors. Second, negative reinforcement entails the *removal* of a negative consequence when functional behaviors are performed; punishment entails the *administration* of negative consequences when dysfunctional behaviors are performed.

social learning theory

A theory that takes into account how learning and motivation are influenced by people's thoughts and beliefs and their observations of other people's behavior.

vicarious learning

Learning that occurs when the learner becomes motivated to perform a behavior by watching another person perform it and be reinforced for doing so; also called *observational learning*.

Social learning theory

Social learning theory proposes that motivation results not only from direct experience of rewards and punishments but also from a person's thoughts and beliefs. Social learning theory extends operant conditioning's contribution to managers' understanding of motivation by explaining (1) how people can be motivated by observing other people perform a behavior and be reinforced for doing so (*vicarious learning*), (2) how people can be motivated to control their behavior themselves (*self-reinforcement*), and (3) how people's beliefs about their ability to successfully perform a behavior affect motivation (*self-efficacy*).⁶⁴ We look briefly at each of these motivators.

VICARIOUS LEARNING **Vicarious learning**, often called *observational learning*, occurs when a person (the learner) becomes motivated to perform a behavior by watching another person (the model) perform the behavior and be positively reinforced for doing so. Vicarious learning is a powerful source of motivation on many jobs in which people learn to perform functional behaviors by watching others. Salespeople learn how to be helpful to customers, medical school students

learn how to treat patients, law clerks learn how to practice law, and non-managers learn how to be managers, in part, by observing experienced members of an organization perform these behaviors properly and be reinforced for them. In general, people are more likely to be motivated to imitate the behavior of models who are highly competent, are (to some extent) experts in the behavior, have high status, receive attractive reinforcers, and are friendly or approachable.⁶⁵

To promote vicarious learning, managers should strive to have the learner meet the following conditions:

- The learner observes the model performing the behavior.
- The learner accurately perceives the model's behavior.
- The learner remembers the behavior.
- The learner has the skills and abilities needed to perform the behavior.
- The learner sees or knows that the model is positively reinforced for the behavior.⁶⁶

SELF-REINFORCEMENT Although managers are often the providers of reinforcement in organizations, sometimes people motivate themselves through self-reinforcement. People can control their own behavior by setting goals for themselves and then reinforcing themselves when they achieve the goals.⁶⁷

Self-reinforcers are any desired or attractive outcomes or rewards that people can give to themselves for good performance, such as a feeling of accomplishment, going to a movie, having dinner out, buying a new CD, or taking time out for a golf game. When members of an organization control their own behavior through self-reinforcement, managers do not need to spend as much time as they ordinarily would trying to motivate and control behavior through the administration of consequences because subordinates are controlling and motivating themselves. In fact, this self-control is often referred to as the *self-management of behavior*.

Chinese students at the prestigious Jiaotong University in Shanghai exemplify how strong motivation through self-control can be. These students, many of whom are aspiring engineers, live in spartan conditions (a barely lit small room is home for seven students) and take exceptionally heavy course loads. They spend their spare time reading up on subjects not covered in their classes, and many ultimately hope to obtain engineering jobs overseas with high-tech companies. Illustrating high self-control, 22-year-old Yan Kangrong spends his spare time reading computer textbooks and designing software for local companies. As Kangrong puts it, "We learn the basics from teachers. . . . But we need to expand on this knowledge by ourselves."⁶⁸

self-reinforcer Any desired or attractive outcome or reward that a person gives to himself or herself for good performance.

self-efficacy A person's belief about his or her ability to perform a behavior successfully.

SELF-EFFICACY **Self-efficacy** is a person's belief about his or her ability to perform a behavior successfully. Even with all the most attractive consequences or reinforcers hinging on high performance, people are not going to be motivated if they do not think that they can actually perform at a high level. Similarly, when people control their own behavior, they are likely to set for themselves difficult goals that will lead to outstanding accomplishments only if they think that they have the capability to reach those goals. Thus, self-efficacy influences motivation both when managers provide reinforcement and when workers themselves provide it.⁶⁹ The greater the self-efficacy, the greater is the motivation and performance.

Pay and Motivation

In Chapter 12, we discussed how managers establish a pay level and structure for an organization as a whole. Here we focus on how, once a pay level and structure are in place, managers can use pay to motivate employees to perform at a high level and attain their work goals. Pay is used to motivate entry-level workers, first-line and middle managers, and even top managers such as CEOs. Pay can be used to motivate people to perform behaviors that help an organization achieve its goals, and it can be used to motivate people to join and remain with an organization.

Each of the theories described in this chapter alludes to the importance of pay and suggests that pay should be based on performance:

- *Expectancy theory.* Instrumentality, the association between performance and outcomes such as pay, must be high for motivation to be high. In addition, pay is an outcome that has high valence for many people.
- *Need theories.* People should be able to satisfy their needs by performing at a high level; pay can be used to satisfy several different kinds of needs.
- *Equity theory.* Outcomes such as pay should be distributed in proportion to inputs (including performance levels).
- *Goal-setting theory.* Outcomes such as pay should be linked to the attainment of goals.
- *Learning theories.* The distribution of outcomes such as pay should be contingent on the performance of organizationally functional behaviors.

As these theories suggest, to promote high motivation, managers should base the distribution of pay to organizational members on performance levels so that high performers receive more pay than low performers (other things being equal).⁷⁰ At General Mills, for example, the pay of all employees, ranging from mailroom clerks to senior managers, is based, at least in part, on performance.⁷¹ A compensation plan basing pay on performance is often called a **merit pay plan**. Once managers have decided to use a merit pay plan, they face two important choices: whether to base pay on individual, group, or organizational performance or to use salary increases or bonuses.

merit pay plan A compensation plan that bases pay on performance.

Basing merit pay on individual, group, or organizational performance

Managers can base merit pay on individual, group, or organizational performance. When individual performance (such as the dollar value of merchandise a salesperson sells, the number of loudspeakers a factory worker assembles, and a lawyer's billable hours) can be accurately determined, individual motivation is likely to be highest when pay is based on individual performance.⁷² When members of an organization work closely together and individual performance cannot be accurately determined (as in a team of computer programmers developing a single software package), pay cannot be based on individual performance, and a group- or organization-based plan must be used. When the attainment of organizational goals hinges on members' working closely together and cooperating with each other (as in a small construction company that builds

custom homes), group- or organization-based plans may be more appropriate than individual-based plans.⁷³

It is possible to combine elements of an individual-based plan with a group- or organization-based plan to motivate each individual to perform highly and, at the same time, motivate all individuals to work well together, cooperate with one another, and help one another as needed. Lincoln Electric, a very successful company and a leading manufacturer of welding machines, uses a combination individual- and organization-based plan.⁷⁴ Pay is based on individual performance. In addition, each year the size of a bonus fund depends on organizational performance. Money from the bonus fund is distributed to people on the basis of their contributions to the organization, attendance, levels of cooperation, and other indications of performance. Employees of Lincoln Electric are motivated to cooperate and help one another because when the firm as a whole performs well, everybody benefits by having a larger bonus fund. Employees also are motivated to contribute their inputs to the organization because their contributions determine their share of the bonus fund.

Salary increase or bonus?

Managers can distribute merit pay to people in the form of a salary increase or a bonus on top of regular salaries. Although the dollar amount of a salary increase or bonus might be identical, bonuses tend to have more motivational impact for at least three reasons. First, salary levels are typically based on performance levels, cost-of-living increases, and so forth, from the day people start working in an organization, which means that the absolute level of the salary is based largely on factors unrelated to *current* performance. A 5 percent merit increase in salary, for example, may seem relatively small in comparison to one's total salary. Second, a current salary increase may be affected by other factors in addition to performance, such as cost-of-living increases or across-the-board market adjustments. Third, because organizations rarely reduce salaries, salary levels tend to vary less than performance levels do. Related to this point is the fact that bonuses give managers more flexibility in distributing outcomes. If an organization is doing well, bonuses can be relatively high to reward employees for their contributions. However, unlike salary increases, bonus levels can be reduced when an organization's performance lags. All in all, bonus plans have more motivational impact than salary increases because the amount of the bonus can be directly and exclusively based on performance.⁷⁵

Consistent with the lessons from motivation theories, bonuses can be linked directly to performance and vary from year to year and employee to employee, as at Gradient Corporation, a Cambridge, Massachusetts, environmental consulting firm.⁷⁶ Another organization that successfully uses bonuses is Nucor Corporation. Steelworkers at Nucor tend to be much more productive than steelworkers in other companies—probably because they can receive bonuses tied to performance and quality that are from 130 to 150 percent of their regular or base pay.⁷⁷

In addition to receiving pay raises and bonuses, high-level managers and executives are sometimes granted employee stock options. **Employee stock options** are financial instruments that entitle the bearer to buy shares of an organization's stock at a certain price during a certain period of time or under certain conditions.⁷⁸ For example, in addition to salaries stock options are sometimes

employee stock option A financial instrument that entitles the bearer to buy shares of an organization's stock at a certain price during a certain period of time or under certain conditions.

used to attract high-level managers. The exercise price is the stock price at which the bearer can buy the stock, and the vesting conditions specify when the bearer can actually buy the stock at the exercise price. The option's exercise price is generally set equal to the market price of the stock on the date it is granted, and the vesting conditions might specify that the manager has to have worked at the organization for 12 months or perhaps met some performance target (increase in profits) before being able to exercise the option. In high-technology firms and start-ups, options are sometimes used in a similar fashion for employees at various levels in the organization.⁷⁹

From a motivation standpoint, stock options are used not so much to reward past individual performance but, rather, to motivate employees to work in the future for the good of the company as a whole. This is true because stock options issued at current stock prices have value in the future only if an organization does well and its stock price appreciates; thus, giving employees stock options should encourage them to help the organization improve its performance over time.⁸⁰ At high-technology start-ups and dot-coms, stock options have often motivated potential employees to leave promising jobs in larger companies and work for the start-ups. In the late 1990s and early 2000s, many dot-commers were devastated to learn not only that their stock options were worthless, because their companies went out of business or were doing poorly, but also that they were unemployed.

Examples of merit pay plans

Managers can choose among several merit pay plans, depending on the work that employees perform and other considerations. Using *piece-rate pay*, an individual-based merit plan, managers base employees' pay on the number of units each employee produces, whether televisions, computer components, or welded auto parts. Managers at Lincoln Electric use piece-rate pay to determine individual pay levels. Advances in information technology are currently simplifying the administration of piece-rate pay in a variety of industries. For example, farmers have typically allocated piece-rate pay to farmworkers through a laborious, time-consuming process. Now, they can rely on metal buttons the size of a dime that farmworkers clip to their shirts or put in their pockets. Made by Dallas Semiconductor Corporation, these buttons are customized for use in farming by Agricultural Data Systems, based in Laguna Niguel, California.⁸¹ Each button contains a semiconductor linked to payroll computers by a wandlike probe in the field.⁸² The wand relays the number of boxes of fruit or vegetables that each worker picks as well as the type and quality of the produce picked, the location it was picked in, and the time and the date. The buttons are activated by touching them with the probe; hence, they are called Touch Memory Buttons. Managers generally find that the buttons save time, improve accuracy, and provide valuable information about their crops and yields.⁸³

Using *commission pay*, another individual-based merit pay plan, managers base pay on a percentage of sales. Managers at the successful real-estate company Re/Max International Inc. use commission pay for their agents, who are paid a percentage of their sales. Some department stores, such as Neiman Marcus, use commission pay for their salespeople.

Examples of organizational-based merit pay plans include the Scanlon plan and profit sharing. The *Scanlon plan* (developed by Joseph Scanlon, a union leader in a

steel and tin plant in the 1920s) focuses on reducing expenses or cutting costs; members of an organization are motivated to come up with and implement cost-cutting strategies because a percentage of the cost savings achieved during a specified time is distributed to the employees.⁸⁴ Under *profit sharing*, employees receive a share of an organization's profits. Approximately 16 percent of the employees in medium or large firms receive profit sharing, and about 25 percent of small firms give their employees a share of the profits.⁸⁵ Regardless of the specific kind of plan that is used, managers should always strive to link pay to the performance of behaviors that help an organization achieve its goals.

Japanese managers in large corporations have long shunned merit pay plans in favor of plans that reward seniority. However, more and more Japanese companies are adopting merit-based pay due to its motivational benefits, such as SiteDesign,⁸⁶ Tokio Marine and Fire Insurance, and Hissho Iwai, a trading organization.⁸⁷

Summary and Review

THE NATURE OF MOTIVATION Motivation encompasses the psychological forces within a person that determine the direction of the person's behavior in an organization, the person's level of effort, and the person's

level of persistence in the face of obstacles. Managers strive to motivate people to contribute their inputs to an organization, to focus these inputs in the direction of high performance, and to ensure that people receive the outcomes they desire when they perform at a high level.

EXPECTANCY THEORY According to expectancy theory, managers can promote high levels of motivation in their organizations by taking steps to ensure that expectancy is high (people think that if they try, they can perform at a high level), instrumentality is high (people think that if they perform at a high level, they will receive certain outcomes), and valence is high (people desire these outcomes).

NEED THEORIES Need theories suggest that to motivate their workforces, managers should determine what needs people are trying to satisfy in organizations and then ensure that people receive outcomes that satisfy these needs when they perform at a high level and contribute to organizational effectiveness.

EQUITY THEORY According to equity theory, managers can promote high levels of motivation by ensuring that people perceive that there is equity in the organization or that outcomes are distributed in proportion to inputs. Equity exists when a person perceives that his or her own outcome-input ratio equals the outcome-input ratio of a referent. Inequity motivates people to try to restore equity.

GOAL-SETTING THEORY Goal-setting theory suggests that managers can promote high motivation and performance by ensuring that people are striving to achieve specific, difficult goals. It is important for people to accept the goals, be committed to them, and receive feedback about how they are doing.

LEARNING THEORIES Operant conditioning theory suggests that managers can motivate people to perform highly by using positive reinforcement or negative reinforcement (positive reinforcement being the preferred strategy). Managers can motivate people to avoid performing dysfunctional behaviors by using extinction or punishment. Social learning theory suggests that people can also be motivated by observing how others perform behaviors and receive rewards, by engaging in self-reinforcement, and by having high levels of self-efficacy.

PAY AND MOTIVATION Each of the motivation theories discussed in this chapter alludes to the importance of pay and suggests that pay should be based on performance. Merit pay plans can be individual-, group-, or organization-based and can entail the use of salary increases or bonuses.



Management in Action

Topics for Discussion and Action

Discussion

1. Discuss why two people with similar abilities may have very different expectancies for performing at a high level.
2. Describe why some people have low instrumentalities even when their managers distribute outcomes based on performance.
3. Analyze how professors try to promote equity to motivate students.

4. Describe three techniques or procedures that managers can use to determine whether a goal is difficult.
5. Discuss why managers should always try to use positive reinforcement instead of negative reinforcement.

Action

6. Interview three people who have the same kind of job (such as salesperson, waiter/waitress, or teacher),

and determine what kinds of needs they are trying to satisfy at work.

7. Interview a manager in an organization in your community to determine the extent to which the manager takes advantage of vicarious learning to promote high motivation among subordinates.

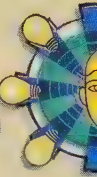


Building Management Skills

Diagnosing Motivation

Think about the ideal job that you would like to obtain upon graduation. Describe this job, the kind of manager you would like to report to, and the kind of organization you would be working in. Then answer the following questions:

1. What would be your levels of expectancy and instrumentality on this job? Which outcomes would have high valence for you on this job? What steps would your manager take to influence your levels of expectancy, instrumentality, and valence?
2. Whom would you choose as a referent on this job? What steps would your manager take to make you feel that you were being equitably treated? What would you do if, after a year on the job, you experienced underpayment inequity?
3. What goals would you strive to achieve on this job? Why? What role would your manager play in determining your goals?
4. What needs would you strive to satisfy on this job? Why? What role would your manager play in helping you satisfy these needs?
5. What behaviors would your manager positively reinforce on this job? Why? What positive reinforcers would your manager use?
6. Would there be any vicarious learning on this job? Why or why not?
7. To what extent would you be motivated by self-control on this job? Why?
8. What would be your level of self-efficacy on this job? Why would your self-efficacy be at this level? Should your manager take steps to boost your self-efficacy? If not, why not? If so, what would these steps be?





Small Group Breakout Exercise

Increasing Motivation

Form groups of three or four people, and appoint one member as the spokesperson who will communicate your findings to the whole class when called on by the instructor. Then discuss the following scenario.

You and your partners own a chain of 15 dry-cleaning stores in a medium-size town. All of you are concerned about a problem in customer service that has surfaced recently. When any one of you spends the day, or even part of the day, in a particular store, clerks seem to provide excellent customer service, spotters are making sure all stains are removed from garments, and pressers are doing a good job of pressing difficult items such as silk blouses. Yet during those same visits customers complain to you about such things as

stains not being removed and items being poorly pressed in some of their previous orders; indeed, several customers have brought garments in to be redone. Customers also sometimes comment on having waited too long for service on previous visits. You and your partners are meeting today to address this problem.

1. Discuss the extent to which you believe that you have a motivation problem in your stores.
2. Given what you have learned in this chapter, design a plan

to increase the motivation of clerks to provide prompt service to customers even when they are not being watched by a partner.

3. Design a plan to increase the motivation of spotters to remove as many stains as possible even when they are not being watched by a partner.
4. Design a plan to increase the motivation of pressers to do a top-notch job on all clothes they press, no matter how difficult.



Be the Manager

You supervise a team of marketing analysts who work on different snack products in a large food products company. The marketing analysts have recently received undergraduate degrees in business or liberal arts and have been on the job between one and three years. Their responsibilities include analyzing the market for their respective products, including competitors; tracking current marketing initiatives; and planning future marketing campaigns. They also need to prepare quarterly sales and expense reports for their products and estimated budgets for the next three quarters; to prepare these reports, they need to obtain data from financial and accounting analysts assigned to their products.

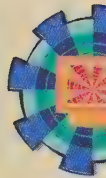
When they first started on the job, you took each marketing analyst through the reporting cycle explaining what needs to be done and how to accomplish it and emphasizing the need for timely reports. While preparing the reports can be tedious, you think the task is pretty straightforward and easily accomplished if the analysts plan ahead and allocate sufficient time for it. When reporting time approaches, you remind the analysts through emails and emphasize the need for accurate and timely reports in team meetings.

You believe that this element of the analysts' jobs couldn't be more straightforward. However, at the end of each quarter, the majority of the analysts turn their reports in a

day or two late, and, worse yet, your own supervisor (whom the reports are eventually turned in to) has indicated that information is often missing and sometimes the reports contain errors. Once you started getting flak from your supervisor about this problem, you decided you better fix things, and quick. You met with the marketing analysts, explained the problem, told them to turn the reports in to you a day or two early so that you could look them over, and more generally emphasized that they really needed to get their act together. Unfortunately, things have not improved much, and you are spending more and more of your own time doing the reports. What are you going to do?

Additional Activities on the Build Your Management Skills DVD

- **Test Your Knowledge:**
(1) Maslow's Hierarchy of Needs, (2) Reinforcement Theory, and (3) Reinforcing Performance
- **Self Assessment:** Assessing How Personality Type Affects Goal-Setting



Managing Ethically

Sometimes pay is so contingent upon performance that it creates stress for employees. Imagine a salesperson who knows that if sales targets are not met, she or he will not be able to make a house mortgage payment or pay the rent.

Questions

1. Either individually or in a group, think about the ethical implications of closely linking pay to performance.
2. Under what conditions might contingent pay be most stressful, and what steps can managers take to try to help their subordinates perform effectively and not experience excessive amounts of stress?



Case for Discussion

Tindell and Boone Inspire and Motivate at the Container Store

How can managers motivate employees in an industry known for high levels of turnover and low levels of motivation?

Kip Tindell and Garrett Boone founded the Container Store in Dallas, Texas, in 1978 and currently serve as CEO and chairman, respectively. When they opened their first store, they were out on the floor trying to sell customers their storage and organization products that would economize on space and time and make purchasers' lives a little less complicated. The Container Store has grown to include 30 stores in eleven states; although the original store in Dallas had only 1,600 square feet, the stores today average around 25,000 square feet.⁸⁸ The phenomenal growth in the size of the stores has been matched by a 20 to 25 percent growth in annual sales.⁸⁹ Surprising enough, Tindell and Boone can still

be found on the shop floor tidying shelves and helping customers carry out their purchases.⁹⁰ And that, perhaps, is an important clue to the secret of their success. The Container Store has been consistently ranked among *Fortune* magazine's "100 Best Companies to Work For" for six years running.⁹¹ In 2005, the Container Store was fifteenth on this list (in 2000 and 2001, it was first; in 2002 and 2003, second; in 2004, third).⁹²

Early on, Tindell and Boone recognized that people are the Container Store's most valuable asset and that after hiring great people, one of the most important managerial tasks is motivating them. One would think that motivating employees might be especially challenging in the retail industry, which has an average annual turnover rate for full-time salespeople of more than 70 percent and an annual turnover

rate for store managers of over 30 percent. The Container Store's comparable figures are fractions of these industry statistics, a testament to Tindell and Boone's ability to motivate.⁹³ As part of the *Fortune* survey, employees were anonymously polled about their trust in management, management's commitment to employees, how they felt about their jobs and working at the Container Store, and their day-to-day work life.⁹⁴ According to survey's findings, morale at the Container Store is "exuberant."⁹⁵

How do Tindell and Boone do it? Essentially, by being clear about what is important at the Container Store, enabling employees to be high performers, rewarding employees in multiple ways, creating a fair and stimulating work environment, and treating employees like the highly capable individuals that they are.⁹⁶ Maintaining customer service



and a motivated, enthusiastic workforce that is treated well are top priorities at the Container Store, as are honesty, openness, and trust.

While the majority of full-time salespeople have college degrees, they nonetheless receive more than 200 hours of training during their first year on the job (compared to an industry average of under 10 hours).⁹⁷ This focus on training continues throughout employees' careers with the Container Store, consistent with Tindell and Boone's emphasis on customer service and employee motivation. Training focuses on the characteristics and advantages of each product, how to sell and provide superior customer service, and how to creatively meet customers' container and storage needs. Thus, employees feel confident that they can help customers—even those with very unusual container needs—and provide truly excellent service.⁹⁸

Tindell and Boone also recognize the importance of rewarding employees for a job well done. For example, starting salaries for salespeople are around \$40,000 and merit pay increases for superior sales performance are about 8 percent per year. To encourage high individual performance as well as teamwork and cooperation, both individual and team-based rewards are utilized at the Container Store.

Some high-performing salespeople earn more than their store managers, which suits the store managers fine as long as equitable procedures are used and rewards are distributed fairly.⁹⁹

Professional development is a valued outcome employees obtain from working at the Container Store. Employees are respected and are given the autonomy to best meet customers' needs however they see fit. Given all the training they receive (over 150 hours per year), employees are confident that they can do this. As Garrett Boone puts it, "Everybody we hire, we hire as a leader. Anybody in our store can take an action that you might think of typically being a manager's action."¹⁰⁰ Thus, employees really have the opportunity to learn and develop on the job, a situation that is somewhat of a rarity in retail sales.

Additionally, employees are treated with respect and have access to what is often privileged information in other companies, such as the amount of annual store sales. Employees also have flexible work options and flexible benefits; medical, dental, and 401k retirement plans; job security; a casual dress code; and access to a variety of wellness programs ranging from yoga classes and chair massages to a personalized, Web-based nu-

trition and exercise planner.¹⁰¹ Equally important is the opportunity to work with other highly motivated individuals in an environment that exudes enthusiasm and excitement. Not only are the Container Store's employees motivated, but they also look forward to coming to work and feel as if their co-workers and managers are part of their family. Employees feel pride in what they do—helping customers organize their lives, save space and time, and have a better sense of well-being. Hence, they not only personally benefit from high performance but also feel good about the products they sell and the help they give customers.¹⁰² Tindell and Boone evidently have never lost sight of the importance of motivation for both organizations and their members.

Questions

1. How does the Container Store motivate its employees?
2. Why are turnover rates lower at the Container Store than at other comparable retail establishments?
3. Why is training considered to be so important at the Container Store?
4. Why do college graduates find it motivating to sell storage and organization products?

BusinessWeek

Case in the News

More than a decade ago, Boeing Co. quietly began investigating an explosive internal issue: whether female employees were paid less than men. Several sophisticated salary studies concluded that the answer was yes. One 1998 report said "men are more likely to

be hired into the high paying positions." A statistical analysis completed the same year noted that the pay gap for entry-level managers was \$3,741.04.

Although she knew nothing of these sensitive analyses, Carol Jensen would not have found them

surprising. The 64-year-old technical drafter had long complained that women were underpaid. "We were treated with little respect," recalls the mother of nine, who started working at Boeing in 1967 and was laid off in 2000. "The men believed that the only work for

Coverup at Boeing?

women at Boeing was behind a desk as a secretary.”

In 2000, 38 women filed a class action in Seattle against the company for pay discrimination. The potential cost to Boeing exceeded \$100 million. All of those salary studies Boeing had done through the years, of course, would have been dynamite evidence for the aggrieved women. But when their lawyers made routine pretrial requests for any statistical data the company might have compiled on gender pay differentials, the aerospace giant said it had no obligation to turn the studies over. Why? Because they had allegedly been prepared at the direction of Boeing’s lawyers and were therefore protected by attorney-client privilege. That’s a legal doctrine that shields confidential communications between executives and their attorneys from public disclosure. It’s intended to allow managers to be candid with their legal counselors.

Behind the scenes, meanwhile, Boeing employees removed payroll-planning documents about pay discrimination from the company’s files. In an e-mail dated August 27, 2001, compensation manager Paul A. Wells advised colleagues to get rid of drafts of these types of documents on the Salary Administration server because “that which is retained can potentially be subpoenaed and . . . those with access [to] the files can be called on to testify about the content.” Wells declined to comment.

Systematic Campaign

It’s a classic scenario—the type of confrontation that has served as dramatic fodder for countless movies: A big, powerful company bullies small, weak individuals. *Erin Brockovich*, *A Civil Action*, and

many other legal thrillers tell this tale from the point of view of the victims. But *BusinessWeek* has obtained a rare view of the other side of the story: what takes place at the company. The federal judge overseeing the class action, Marsha J. Pechman, agreed to unseal more than 12,000 pages of internal Boeing documents on February 11 after *BusinessWeek* attorneys argued that they should be disclosed. This hidden corporate history raises questions as to whether the company and its lawyers engaged in a systematic campaign to hide evidence and take advantage of attorney-client privilege.

Having witnessed Boeing’s intransigence for more than four years, highlighted by a ferocious battle to avoid disclosure of its salary studies, Judge Pechman dropped an even bigger bombshell on the company on May 11. Citing “an evolving awareness, as more facts come to light, of how Boeing had inappropriately tried to shield [the documents] from discovery,” she ordered Boeing to hand over the series of salary analyses it had fought hardest to withhold—ones that left little room for doubting the company’s knowledge of its pay disparities. That was only one of several rebukes Boeing received from the judge, as well as from a special master assigned to referee discovery disputes, during the course of the lawsuit. Though many questions remain about the company’s conduct during the case, and a complete picture of the role played by Boeing’s various managers and lawyers is still unavailable, Judge Pechman’s rulings suggest that the company went beyond standard aggressive legal defense tactics.

Now that Boeing was faced with the prospect of telling jurors why its own internal documents seemingly

contradicted its legal theory, the company suddenly became accommodating. Two days before the case was scheduled to go to trial, on May 17, Boeing made a settlement offer. While the two teams hammer out the details of the deal, which neither side will discuss, the case has been postponed. . . .

Spokesman Kenneth B. Mercer says Boeing is committed to honest business practices and equal opportunity. Because settlement talks in the Beck lawsuit aren’t complete, he refuses to discuss the underlying facts of the case, the conduct of the company’s attorneys, or any of the individual documents obtained by *BusinessWeek*—beyond saying Boeing thinks its hiring and promotion practices are fair. Mercer adds that the statistical studies Judge Pechman forced the company to turn over were intended to help eliminate pay disparities and that they “can’t capture all of the critical factors that go into pay or promotion decisions.”

Boeing’s Mercer also noted that federal judge’s have tossed out three similar gender-discrimination class actions filed against Boeing in Southern California, Kansas, and Missouri. A fourth suit, in Oklahoma, has been granted class-action status. The company says its high batting average against female pay-discrimination suits is proof that its compensation practices were legal. But plaintiffs’ attorneys claim Boeing won mainly because it successfully suppressed the evidence that ultimately entered the Beck case.

Record Output of Jets

Troubling headlines are a comparatively new problem for Boeing. A company dominated by engineers, it traditionally focused on innovation

and design. Executives believed that profits would naturally follow. During the Pentagon overbilling scandals of the late 1980s, Boeing was the least tarnished of the major contractors. But the culture started changing after its merger with the more aggressive McDonnell Douglas in 1997. That deal, along with tougher competition for government dollars in the Clinton years, shifted Boeing's emphasis to the bottom line.

Women first entered Boeing's workforce in large numbers during World War II—and they enabled the company to roll out record fleets of B-17 bombers. But when the war ended, Boeing's male-dominated culture returned in full force. When Carol Jensen joined in 1967, she was one of the first females to draw technical blueprints. "Men were getting the plum designing assignments," recalls Jensen. "It was out-and-out discrimination, and a woman couldn't do anything about it."

Despite the anger of Jensen and others, female pay didn't become a serious concern at Boeing until 1996, when the Labor Dept.'s Office of Federal Contract Compliance Program (OFCCP) ran a routine investigation of Boeing's mammoth Philadelphia plant. Under government contracting rules, the OFCCP has the right to audit whether federal contractors are complying with anti-discrimination laws. The agency does this by using a statistical method known as "median analysis." In broad terms, it compares the relationship between the median pay of male and female employees and their median job experience.

After informing Boeing that the OFCCP had discovered "a prima facie case of systemic discrimination concerning compensation of females and minorities" in Philadel-

phia, the agency audited nine other plants nationwide. The stakes for Boeing, the country's No. 2 federal contractor, were huge. With defense and space representing nearly half of its revenues and growing, the loss of federal contracts would be devastating.

Recognizing the seriousness of the inquiry, Boeing wasted no time launching a counterattack. It hired Jon A. Geier, a partner in the Washington (D.C.) office of Paul, Hastings, Janofsky & Walker LLP. One of his top priorities, Geier said in a declaration submitted in the Beck case, was to develop a "legally defensible" statistical analysis of Boeing's pay practices to counter the one OFCCP used to evaluate pay discrimination. But there was one big problem: The findings of Geier's own Diversity Salary Analysis project, or DSA, also found pay disparities. Its 1997 report determined that females "are paid less." The next year's report noted that "gender differences in starting salaries generally continue and often increase as a result of salary planning decisions." Geier did not respond to requests for comment. . . .

"There Was a Lot More"

Despite Boeing's "extensive efforts," in the words of one in-house lawyer, not to forfeit the attorney-client privilege, the company did do a few things to jeopardize its eligibility for that legal protection. Its attorneys, for instance, gave DSA documents to managers outside their tightly guarded legal team. These execs used the information not just to fight the OFCCP inquiry but also to make broader salary decisions.

The OFCCP settled with Boeing for \$4.5 million in November 1999.

Boeing did not admit liability. On December 1, relieved human-resource execs and attorneys gathered to discuss their victory over the federal government, according to a meeting transcription obtained by *BusinessWeek*. Boeing's former director for employee relations, Marcella Fleming, declared that the company got off easy. "We thought that there was a lot more potential financial liability out there," Fleming told her colleagues. "And so, what we're paying for this deal in the long run is a lot less than we think we could have potentially paid." Fleming declined to comment for this story.

Boeing officials had little time to dwell on their triumph. On February 25, 2000, Seattle attorney Michael D. Helgren filed the Beck v. Boeing class action after some female employees told him their stories. The company enlisted the help of its chief outside law firm, Seattle-based Perkins Cole LLP. . . .

Almost immediately, the company resumed the aggressive strategies that had worked so well in the OFCCP investigation. After being deposed by attorney Helgren in September 2000, Boeing compensation manager Jeffrey K. Janders told colleagues in a memo that he wanted the Salary Planning Team to "delete the concept of target salaries"—the hypothetical pay increases Boeing executives believed would be necessary to create salary parity—"to prevent an audit trail where a substantial difference exists between target and planned salaries." Because Janders could not be reached for comment, *BusinessWeek* does not know the full context of the e-mail.

Helgren did not find out about these maneuvers until years later, but from the start he suspected that the company was not turning over all of the salary information it had.

After Boeing's Hannah claimed that many of the pay-related documents his rival wanted were covered by attorney-client privilege, Helgren requested a so-called privilege log—a list containing a brief description of every document the company was withholding. A common tool in U.S. courts, these logs are intended to give plaintiffs' attorneys an idea of what material the defendant is holding back and why it is privileged without revealing any sensitive secrets. . . .

Suspecting that many of these documents did not deserve attorney-client privilege, Helgren asked for a judicial review of those covered by the privilege log. Judge Pechman assigned retired state court judge George Finkle the job of managing pretrial discovery disputes. After studying a 1,400-page sample of Boeing's DSA documents, Finkle rejected the claim that the studies were protected simply because attorneys were involved in producing them. The documents "served business purposes extending well beyond providing assistance in . . . anticipation of litigation," Finkle ruled on October 25, 2000. "Legal departments are not citadels in which public business or technical information may be placed to defeat discovery and thereby ensure confidentiality."

That should have been the end of Helgren's quest. Still, Boeing dragged its feet. The documents Judge Finkle ordered Boeing to give to plaintiffs' attorneys came slowly and in small batches. It wasn't until early 2004 that Boeing attorneys handed over some damning internal statistical salary studies that execs had not even previously acknowledged. For Helgren, these late-released documents proved Boeing not only knew about the pay discrimination but refused to take serious steps to eliminate it. "These pay disparities were caused by their own practices," Helgren says. "None of this was by chance. And they continued for years and years to avoid the problem."

Suddenly Amenable

In a last-ditch effort to prevent a jury from seeing these potential smoking guns, Boeing attorneys appealed Finkle's discovery order. They claimed that disclosing these documents would "materially and unfairly" bias the case. On March 11, Pechman denied Boeing's appeal. It was a huge boost for Helgren, who started gearing up for the trial, scheduled to begin on May 17. But on May 13, he got an unexpected call. A third party representing Boeing phoned to say the

company was willing to talk settlement. Negotiations proceeded almost continuously until the next day at noon, when the two sides reached a tentative settlement.

While she is happy about the potential deal, plaintiff Jensen is reserving judgment about the company. Among her nine children are six adult daughters, and she currently "wouldn't let any of them work at Boeing." The pay gap there may disappear one day. But one thing Boeing will never be able to erase is its long history of underpaying women.

Questions

1. What inequities did women and minorities at Boeing experience?
2. What were the consequences of these inequities?
3. When managers became aware of the inequities, what did they do? Why didn't they do more?
4. What are the broader implications of the discrimination suits for Boeing and its future?

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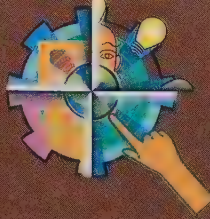
CHAPTER 10

Leaders and Leadership

Learning Objectives

After studying this chapter, you should be able to:

- Describe what leadership is, when leaders are effective and ineffective, and the sources of power that enable managers to be effective leaders.
- Identify the traits that show the strongest relationship to leadership, the behaviors leaders engage in, and the limitations of the trait and behavior models of leadership.
- Explain how contingency models of leadership enhance our understanding of effective leadership and management in organizations.
- Describe what transformational leadership is, and explain how managers can engage in it.
- Characterize the relationship between gender and leadership.



Management Snapshot

John Mackey's Personal Leadership Style

What role does a leader's personal leadership style play in an organization?

John Mackey cofounded the Whole Foods Market in 1980 with two former partners in a 10,000-square-foot location in Austin, Texas, and is the company's current CEO and president. Today, with 168 stores and 32,000 employees, Whole Foods is included in the Fortune 500 list of the biggest companies in America (in terms of size, Whole Foods moved up from being 508 on the list in 2004 to being 479 in 2005).¹ Whole Foods started out to promote healthy eating, and in its early days, the stores were dominated by nuts, grains, and fresh produce. The stores today stock all sorts of food products as long as they are healthy; Whole Food does not carry food containing trans fats, artificial colors or flavors, or chemical preservatives or made from animals that are not treated humanely.²

Mackey is casual and informal but also opinionated, blunt, and direct.³ He combines good business sense and an eye for the bottom line with spirituality and ethical values.

Whole Foods markets tend to have profit margins and prices that are higher than those of typical grocery stores; Mackey is a firm believer in the merits of capitalism and making money. On the spiritual side, he has indicated that "love is the only reality. Everything else is merely a dream or illusion."⁴

Mackey's opinionated and direct nature carries over into the ethical values he promotes at Whole Foods. While acknowledging that Whole Foods has multiple stakeholders, he maintains that the interests of customers and employees come before the interest of shareholders and

that the local community and the natural environment are important stakeholders for Whole Foods. While Mackey is against labor



Whole Foods CEO John Mackey combines good business sense and an eye for the bottom line with spirituality and ethical values.

unions, he is employee-focused and strives to treat employees well and make sure they are satisfied with their jobs (employees are called “team members”).⁵ In 2005, Whole Foods was ranked 30 in *Fortune*’s “100 Best Companies to Work For” (www.fortune.com, 2005; www.wholefoods.com, 2005). Mackey does not believe in huge pay differentials between top managers and rank-and-file team members; at Whole Foods, no salary can be set higher than 14 times that of the average team member, and 94 percent of the stock options that Whole Foods gives to its team members are granted to nonexecutives. Five percent of Whole Foods’ profits each year are donated to charity, and Whole Foods pays its team members for performing community service.⁶

Whole Foods’ mission, the company’s Declaration of Interdependence, was formulated in 1985 by Mackey and around 60 team members during a series of weekend retreats and was revised once in the 1980s and twice in the 1990s.⁷ The declaration

emphasizes interdependence among multiple stakeholders—including customers, team members, shareholders, communities, the natural environment, and business partners—in helping Whole Foods live up to its motto of “Whole Foods, Whole People, Whole Planet.”⁸ Prominent themes in the declaration are high quality; customer satisfaction; frequent, open, and honest communication; team-member happiness and fulfillment; the embracing of diversity; community involvement; and active support of environmental sustainability. The Declaration of Interdependence, or parts of it, not only is espoused by team members but is visible in Whole Foods stores on posters and in free pamphlets. Even so, Whole Foods acknowledges that things might not always be just as they should be at the company and that working and living by the declaration’s principles is a work in progress.⁹ What is never in question is Mackey’s passion to pursue what he believes in.

Overview

John Mackey exemplifies the many facets of effective leadership. In Chapter 1 we explained that one of the four primary tasks of managers is leading. Thus, it should come as no surprise that leadership is a key ingredient in effective management. When leaders are effective, their subordinates or followers are highly motivated, committed, and high-performing. When leaders are ineffective, chances are good that their subordinates do not perform up to their capabilities, are demotivated, and may be dissatisfied as well. CEO Mackey is a leader at the very top of an organization, but leadership is an important ingredient for managerial success at all levels of organizations: top management, middle management, and first-line management. Moreover, leadership is a key ingredient for managerial success for organizations large and small.

In this chapter we describe what leadership is and examine the major leadership models that shed light on the factors that contribute to a manager’s being an effective leader. We look at trait and behavior models, which focus on what leaders are like and what they do, and contingency models—Fiedler’s contingency model, path-goal theory, and the leader substitutes model—each of which takes into account the complexity surrounding leadership and the role of the situation in leader effectiveness. We also describe how managers can use transformational leadership to dramatically affect their organizations. By the end of this chapter, you will have a good appreciation of the many factors and issues that managers face in their quest to be effective leaders.

The Nature of Leadership

leadership The process by which an individual exerts influence over other people and inspires, motivates, and directs their activities to help achieve group or organizational goals.

leader An individual who is able to exert influence over other people to help achieve group or organizational goals.

Leadership is the process by which a person exerts influence over other people and inspires, motivates, and directs their activities to help achieve group or organizational goals.¹⁰ The person who exerts such influence is a **leader**.

When leaders are effective, the influence they exert over others helps a group or organization achieve its performance goals. When leaders are ineffective, their influence does not contribute to, and often detracts from, goal attainment. As the “Management Snapshot” makes clear, John Mackey is taking multiple steps to inspire and motivate Whole Foods employees and direct them to achieve Whole Foods’ goals.

Beyond facilitating the attainment of performance goals, effective leadership increases an organization’s ability to meet all the contemporary challenges discussed throughout this book, including the need to obtain a competitive advantage, the need to foster ethical behavior, and the need to manage a diverse workforce fairly and equitably. Leaders who exert influence over organizational members to help meet these goals increase their organizations’ chances of success.

In considering the nature of leadership, we first look at leadership styles and how they affect managerial tasks and at the influence of culture on leadership styles. We then focus on the key to leadership, power, which can come from a variety of sources. Finally, we consider the contemporary dynamic of empowerment and how it relates to effective leadership.

Personal leadership style and managerial tasks

A manager’s *personal leadership style*—that is, the specific ways in which a manager chooses to influence other people—shapes the way that manager approaches planning, organizing, and controlling (the other principal tasks of managing). Consider John Mackey’s personal leadership style in the “Management Snapshot”: He is casual and informal yet opinionated and direct. While he is concerned with the bottom line, he promotes ethical values and puts the interests of customers and employees before the interests of shareholders. Healthy products, the natural environment, and local communities are important to Mackey, as is the well-being of employees. John Mackey takes active steps to promote the interests of Whole Foods’ multiple stakeholders.

Managers at all levels and in all kinds of organizations have their own personal leadership styles that determine not only how they lead their subordinates but also how they perform the other management tasks. Michael Kraus, owner and manager of a dry-cleaning store in the northeastern United States, for example, takes a hands-on approach to leadership. He has the sole authority for determining work schedules and job assignments for the 15 employees in his store (an organizing task), makes all important decisions by himself (a planning task), and closely monitors his employees’ performance and rewards top performers with pay increases (a control task). Kraus’s personal leadership style is effective in his organization. His employees are generally motivated, perform well, and are satisfied, and his store is highly profitable.

Developing an effective personal leadership style often is a challenge for managers at all levels in an organization. This challenge is often exacerbated when times are tough, due, for example, to an economic downturn or a decline in



Keith Chong hangs up a freshly pressed shirt at his dry-cleaning business in Glendale, California. As owner and manager of a dry-cleaning business, Chong takes a hands-on approach to leadership.

customer demand. The dot-com bust and the slowing economy in the early 2000s provided many leaders with just such a challenge.

While leading is one of the four principal tasks of managing, a distinction is often made between managers and leaders. When this distinction is made, managers are thought of as those organizational members who establish and implement procedures and processes to ensure smooth functioning and who are accountable for goal accomplishment.¹¹ Leaders look to the future, chart the course for the organization, and attract, retain, motivate, inspire, and develop relationships with employees based on trust and mutual respect.¹² Leaders provide meaning and purpose, seek innovation rather than stability, and impassion employees to work together to achieve the leaders' vision.¹³

Leadership styles across cultures

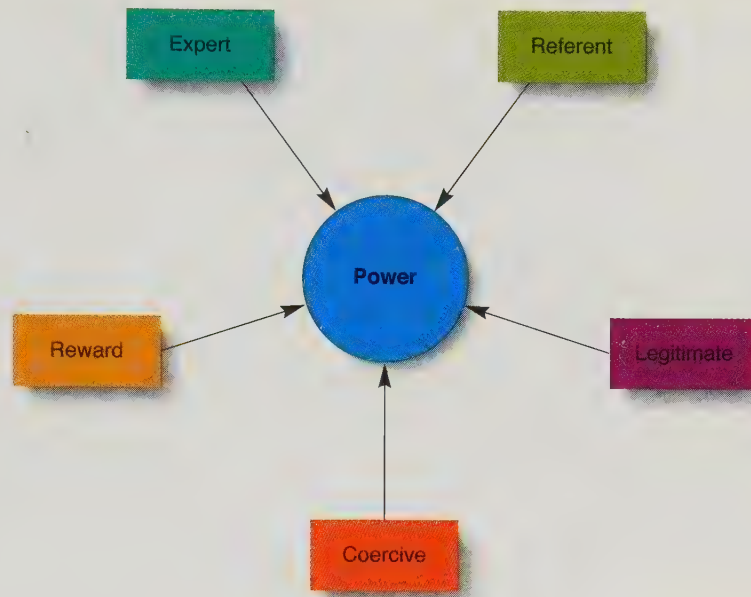
Some evidence suggests that leadership styles vary not only among individuals but also among countries or cultures. Some research indicates that European managers tend to be more humanistic or people-oriented than both Japanese and American managers. The collectivistic culture in Japan places prime emphasis on the group rather than the individual, so the importance of individuals' own personalities, needs, and desires is minimized. Organizations in the United States tend to be very profit-oriented and thus tend to downplay the importance of individual employees' needs and desires. Many countries in Europe have a more individualistic perspective than Japan and a more humanistic perspective than the United States, and this may result in some European managers' being more people-oriented than their Japanese or American counterparts. European managers, for example, tend to be reluctant to lay off employees, and when a layoff is absolutely necessary, they take careful steps to make it as painless as possible.¹⁴

Another cross-cultural difference occurs in time horizons. Managers in any one country often differ in their time horizons, but there are also cultural differences. For example, U.S. organizations tend to have a short-run profit orientation, and thus U.S. managers' personal leadership styles emphasize short-run performance. Japanese organizations tend to have a long-run growth orientation, so Japanese managers' personal leadership styles emphasize long-run performance. Justus Mische, a personnel manager at the European organization Hoechst, suggests that "Europe, at least the big international firms in Europe, have a philosophy between the Japanese, long term, and the United States, short term."¹⁵ Research on these and other global aspects of leadership is in its infancy; as it continues, more cultural differences in managers' personal leadership styles may be discovered.

Power: The key to leadership

No matter what one's leadership style, a key component of **effective leadership** is found in the **power** the leader has to affect other people's behavior and get them to act in certain ways.¹⁶ There are several types of power: **legitimate**, **reward**, **coercive**,

Figure 10.1
Sources of
Managerial
Power



expert, and referent power (see Figure 10.1).¹⁷ Effective leaders take steps to ensure that they have sufficient levels of each type and that they use the power they have in beneficial ways.

legitimate power

The authority that a manager has by virtue of his or her position in an organization's hierarchy.

LEGITIMATE POWER **Legitimate power** is the authority a manager has by virtue of his or her position in an organization's hierarchy. Personal leadership style often influences how a manager exercises legitimate power. Take the case of Carol Loray, who is a first-line manager in a greeting card company and leads a group of 15 artists and designers. Loray has the legitimate power to hire new employees, assign projects to the artists and designers, monitor their work, and appraise their performance. She uses this power effectively. She always makes sure that her project assignments match the interests of her subordinates as much as possible so that they will enjoy their work. She monitors their work to make sure they are on track but does not engage in close supervision, which can hamper creativity. She makes sure her performance appraisals are developmental, providing concrete advice for areas where improvements could be made. Recently, Loray negotiated with her manager to increase her legitimate power so that now she can initiate and develop proposals for new card lines.

reward power The ability of a manager to give or withhold tangible and intangible rewards.

REWARD POWER **Reward power** is the ability of a manager to give or withhold tangible rewards (pay raises, bonuses, choice job assignments) and intangible rewards (verbal praise, a pat on the back, respect). As you learned in Chapter 9, members of an organization are motivated to perform at a high level by a variety of rewards. Being able to give or withhold rewards based on performance is a major source of power that allows managers to have a highly motivated workforce. Managers of salespeople in retail organizations like Neiman Marcus and Dillard's Department Stores, in car dealerships like DaimlerChrysler and Ford, and in travel agencies like Liberty Travel and the Travel Company often use their reward power to motivate their subordinates. Subordinates in organizations such as these often receive commissions on whatever they sell and rewards for the quality of their customer service, which motivate them to do the best they can.

Effective managers use their reward power in such a way that subordinates feel that their rewards signal that they are doing a good job and their efforts are appreciated. Ineffective managers use rewards in a more controlling manner (wielding the “stick” instead of offering the “carrot”) that signals to subordinates that the manager has the upper hand. Managers also can take steps to increase their reward power.

coercive power

The ability of a manager to punish others.

COERCIVE POWER Coercive power is the ability of a manager to punish others. Punishment can range from verbal reprimands to reductions in pay or working hours to actual dismissal. In Chapter 9, we discussed how punishment can have negative side effects such as resentment and retaliation and should be used only when necessary (for example, to curtail a dangerous behavior). Managers who rely heavily on coercive power tend to be ineffective as leaders and sometimes even get fired themselves. William J. Fife is one example; he was fired from his position as CEO of Giddings and Lewis Inc., a manufacturer of factory equipment, because of his overreliance on coercive power. In meetings, Fife often verbally criticized, attacked, and embarrassed top managers. Realizing how destructive Fife’s use of punishment was for them and the company, these managers complained to the board of directors, who, after a careful consideration of the issues, asked Fife to resign.¹⁸

Excessive use of coercive power seldom produces high performance and is questionable ethically. Sometimes it amounts to a form of mental abuse, robbing workers of their dignity and causing excessive levels of stress. Overuse of coercive power can even result in dangerous working conditions. Better results and, importantly, an ethical workplace that respects employee dignity can be obtained by using reward power.

expert power

Power that is based on the special knowledge, skills, and expertise that a leader possesses.

EXPERT POWER Expert power is based on the special knowledge, skills, and expertise that a leader possesses. The nature of expert power varies, depending on the leader’s level in the hierarchy. First-level and middle managers often have technical expertise relevant to the tasks that their subordinates perform. Their expert power gives them considerable influence over subordinates.

Some top managers derive expert power from their technical expertise. Craig Barret, CEO of Intel, has a PhD in materials science from Stanford University and is very knowledgeable about the ins and outs of Intel’s business-producing semiconductors and microprocessors.¹⁹ Similarly, Bill Gates, chairman of Microsoft, and Microsoft CEO Steve Ballmer have expertise in software design; and Tachi Yamada, executive director and chairman of research and development at GlaxoSmithKline (profiled in the “Case for Discussion” in Chapter 5), has an MD and was an active researcher and chairman of the Internal Medicine Department of the University of Michigan Medical School. Many top-level managers, however, lack technical expertise and derive their expert power from their abilities as decision makers, planners, and strategists. Jack Welch, the former, well-known leader and CEO of General Electric, summed it up this way: “The basic thing that we at the top of the company know is that we don’t know the business. What we have, I hope, is the ability to allocate resources, people, and dollars.”²⁰

Effective leaders take steps to ensure that they have an adequate amount of expert power to perform their leadership roles. They may obtain additional training or education in their fields, make sure they keep up to date with the latest developments and changes in technology, stay abreast of changes in their fields through involvement in professional associations, and read widely to be aware of momentous changes in the

referent power

Power that comes from subordinates' and co-workers' respect, admiration, and loyalty.

organization's task and general environments. Expert power tends to be best used in a guiding or coaching manner rather than in an arrogant, high-handed manner.

REFERENT POWER Referent power is more informal than the other kinds of power. Referent power is a function of the personal characteristics of a leader; it is the power that comes from subordinates' and co-workers' respect, admiration, and loyalty. Leaders who are likable and whom subordinates wish to use as a role model are especially likely to possess referent power. Rochelle Lazarus, a top manager at the advertising agency Ogilvy & Mather, won IBM's worldwide advertising account in part because of her referent power.²¹

In addition to being a valuable asset for top managers like Lazarus, referent power can help first-line and middle managers be effective leaders as well. Sally Carruthers, for example, is the first-level manager of a group of secretaries in the finance department of a large state university. Carruthers's secretaries are known to be among the best in the university. Much of their willingness to go above and beyond the call of duty has been attributed to Carruthers's warm and caring nature, which makes each of them feel important and valued. Managers can take steps to increase their referent power, such as taking time to get to know their subordinates and showing interest in and concern for them.

Empowerment: An ingredient in modern management

empowerment

Expanding employees' tasks and responsibilities.

More and more managers today are incorporating into their personal leadership styles an aspect that at first glance seems to be the opposite of being a leader. In Chapter 1, we described how **empowerment**—the process of giving employees at all levels in the organization the authority to make decisions, be responsible for their outcomes, improve quality, and cut costs—is becoming increasingly popular in organizations. When leaders empower their subordinates, the subordinates typically take over some of the responsibilities and authority that used to reside with the leader or manager, such as the right to reject parts that do not meet quality standards, the right to check one's own work, and the right to schedule work activities. Empowered subordinates are given the power to make some of the decisions that their leaders or supervisors used to make.

Empowerment might seem to be the opposite of effective leadership because managers are allowing subordinates to take a more active role in leading themselves. In actuality, however, empowerment can contribute to effective leadership for several reasons:

- Empowerment increases a manager's ability to get things done because the manager has the support and help of subordinates who may have special knowledge of work tasks.
- Empowerment often increases workers' involvement, motivation, and commitment, and this helps ensure that they are working toward organizational goals.
- Empowerment gives managers more time to concentrate on their pressing concerns because they spend less time on day-to-day supervisory activities.

Effective managers realize the benefits of empowerment. The personal leadership style of managers who empower subordinates often entails developing subordinates' ability to make good decisions as well as being their guide, coach, and

source of inspiration. Empowerment is a popular trend in the United States at companies as diverse as United Parcel Service (a package delivery company) and Coram Healthcare Corporation (a provider of medical equipment and services). Empowerment is also taking off around the world.²² For instance, companies in South Korea (such as Samsung, Hyundai, and Daewoo), in which decision making typically was centralized with the founding families, are now empowering managers at lower levels to make decisions.²³

Trait and Behavior Models of Leadership

Leading is such an important process in all organizations—nonprofit organizations, government agencies, and schools, as well as for-profit corporations—that it has been researched for decades. Early approaches to leadership, called the *trait model* and the *behavior model*, sought to determine what effective leaders are like as people and what they do that makes them so effective.

The trait model

The trait model of leadership focused on identifying the personal characteristics that cause effective leadership. Researchers thought effective leaders must have certain personal qualities that set them apart from ineffective leaders and from people who never become leaders. Decades of research (beginning in the 1930s) and hundreds of studies indicate that certain personal characteristics do appear to be associated with effective leadership. (See Table 10.1 for a list of these.)²⁴ Notice that although this model is called the “trait” model, some of the personal characteristics that it identifies are not personality traits per se but, rather, are concerned with a leader’s skills, abilities, knowledge, and expertise. Leaders who do not possess these traits may be ineffective.

Traits alone are not the key to understanding leader effectiveness, however. Some effective leaders do not possess all of these traits, and some leaders who do

Table 10.1

Traits and Personal Characteristics Related to Effective Leadership

Trait	Description
Intelligence	Helps managers understand complex issues and solve problems
Knowledge and expertise	Helps managers make good decisions and discover ways to increase efficiency and effectiveness
Dominance	Helps managers influence their subordinates to achieve organizational goals
Self-confidence	Contributes to managers’ effectively influencing subordinates and persisting when faced with obstacles or difficulties
High energy	Helps managers deal with the many demands they face
Tolerance for stress	Helps managers deal with uncertainty and make difficult decisions
Integrity and honesty	Helps managers behave ethically and earn their subordinates’ trust and confidence
Maturity	Helps managers avoid acting selfishly, control their feelings, and admit when they have made a mistake

possess them are not effective in their leadership roles. This lack of a consistent relationship between leader traits and leader effectiveness led researchers to shift their attention away from traits and to search for new explanations for effective leadership. Rather than focusing on what leaders are like (the traits they possess), researchers began looking at what effective leaders actually do—in other words, at the behaviors that allow effective leaders to influence their subordinates to achieve group and organizational goals.

The behavior model

After extensive study in the 1940s and 1950s, researchers at Ohio State University identified two basic kinds of leader behaviors that many leaders in the United States, Germany, and other countries engaged in to influence their subordinates: consideration and initiating structure.²⁵

consideration

Behavior indicating that a manager trusts, respects, and cares about subordinates.

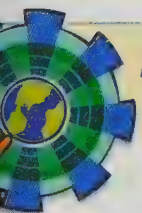
initiating structure

Behavior that managers engage in to ensure that work gets done, subordinates perform their jobs acceptably, and the organization is efficient and effective.

CONSIDERATION Leaders engage in **consideration** when they show their subordinates that they trust, respect, and care about them. Managers who truly look out for the well-being of their subordinates and do what they can to help subordinates feel good and enjoy their work perform consideration behaviors.

INITIATING STRUCTURE Leaders engage in **initiating structure** when they take steps to make sure that work gets done, subordinates perform their jobs acceptably, and the organization is efficient and effective. Assigning tasks to individuals or work groups, letting subordinates know what is expected of them, deciding how work should be done, making schedules, encouraging adherence to rules and regulations, and motivating subordinates to do a good job are all examples of initiating structure.²⁶ Michael Teckel, the manager of an upscale store selling imported men's and women's shoes in a midwestern city, engages in initiating structure when he establishes weekly work, lunch, and break schedules to ensure that the store has enough salespeople on the floor. Teckel also initiates structure when he discusses the latest shoe designs with his subordinates so that they are knowledgeable with customers, when he encourages adherence to the store's refund and exchange policies, and when he encourages his staff to provide high-quality customer service and to avoid a hard-sell approach.

Initiating structure and consideration are independent leader behaviors. Leaders can be high on both, low on both, or high on one and low on the other. As indicated in the following "Managing Globally," many effective leaders like Fujio Cho of Toyota engage in both of these behaviors.



Managing Globally

Toyota Is on a Roll

Toyota president Fujio Cho is driven by speed and flexibility; cost-efficient and flexible production lines that can switch between multiple car models to meet changes in customer demand are his mantra. Toyota is close to becoming the third-largest automobile manufacturer in the United States (Daimler-Chrysler currently has the number-three spot), has sales of over \$140 billion, and has better profit margins than General Motors, Ford, and Daimler-Chrysler.²⁷ Cho is leading a major transformation of Toyota to develop a global, flexible manufacturing system for making cars at record speed, with minimal defects, and in a

cost-effective manner. And Toyota has \$30 billion in cash and securities to weather any unforeseen problems. As Cho puts it, "This is a company that does not fear failure."²⁸ By all counts, Cho is effectively leading Toyota on a path to dominate the global car industry.²⁹

Cho emphasizes consideration in his modest, cheerful approach to being on top of every problem and issue that Toyota faces. He is down to earth and genial. When he led the opening of Toyota's biggest factory in Georgetown, Kentucky, he often worked alongside employees on the factory floor and expressed appreciation for the work that they were doing. He also became involved in the local community and was a speaker at Rotary Club meetings. His concern for people shows through in the smile that often graces his face and in his affable manner of dealing with employees and letting them know he respects and cares about them.³⁰

Cho has been engaging in initiating structure as he leads Toyota toward the goal of having 15 percent of total global automobile sales by 2010. For example,



Toyota President Fujio Cho has set aggressive goals for the company (initiating structure), while also showing employees that he respects and cares about them (consideration).

he spearheaded a program with suppliers to dramatically reduce the number of steps in making car parts and cars and has reduced Toyota's costs (without layoffs or plant shut-downs) by over \$2.5 billion. The flexible, global manufacturing system he is developing will enable Toyota factories around the world to both customize cars for their local markets and make cars for other markets where customer demand exceeds supply, all in a speedy, cost-efficient manner. Cho instituted Toyota's Construction of Cost Competitiveness for the 21st Century (CCC21) program with the goal of reducing prices of components for new car models by 30 percent. *Kaizen*, Toyota's renowned system of continuous improvement, is being taken to another level by Cho, who is striving to make each and every Toyota plant capable of producing high-quality vehicles at low costs.³¹ All in all, Cho's consideration and initiating structure are helping transform Toyota into a carmaker to be reckoned with.

You might expect that effective leaders and managers would perform both kinds of behaviors, but research has found that this is not necessarily the case. The relationship between performance of consideration and initiating-structure behaviors and leader effectiveness is not clear-cut. Some leaders are effective even when they do not perform consideration or initiating-structure behaviors, and some leaders are ineffective even when they do perform both kinds of behaviors. Like the trait model of leadership, the behavior model alone cannot explain leader effectiveness. Realizing this, researchers began building more complicated models of leadership, models focused not only on the leader and what he or she does but also on the situation or context in which leadership occurs.

Contingency Models of Leadership

Simply possessing certain traits or performing certain behaviors does not ensure that a manager will be an effective leader in all situations calling for leadership. Some managers who seem to possess the “right” traits and perform the “right” behaviors turn out to be ineffective leaders. Managers lead in a wide variety of situations and organizations and have various kinds of subordinates performing diverse tasks in a multiplicity of environmental contexts. Given the wide variety of situations in which leadership occurs, what makes a manager an effective leader in one situation (such as certain traits or certain behaviors) is not necessarily what that manager needs to be equally effective in a different situation. An effective army general might not be an effective university president; an effective manager of a restaurant might not be an effective manager of a clothing store; an effective coach of a football team might not be an effective manager of a fitness center; and an effective first-line manager in a manufacturing company might not be an effective middle manager. The traits or behaviors that may contribute to a manager’s being an effective leader in one situation might actually result in the same manager being an ineffective leader in another situation.

Contingency models of leadership take into account the situation or context within which leadership occurs. According to contingency models, whether or not a manager is an effective leader is the result of the interplay between what the manager is like, what he or she does, and the situation in which leadership takes place. Contingency models propose that whether a leader who possesses certain traits or performs certain behaviors is effective depends on, or is contingent on, the situation or context. In this section, we discuss three prominent contingency models developed to shed light on what makes managers effective leaders: Fred Fiedler’s contingency model, Robert House’s path-goal theory, and the leader substitutes model. As you will see, these leadership models are complementary; each focuses on a somewhat different aspect of effective leadership in organizations.

Fiedler’s contingency model

Fred E. Fiedler was among the first leadership researchers to acknowledge that effective leadership is contingent on, or depends on, the characteristics of the leader *and* of the situation. Fiedler’s contingency model helps explain why a manager may be an effective leader in one situation and ineffective in another; it also suggests which kinds of managers are likely to be most effective in which situations.³²

LEADER STYLE As with the trait approach, Fiedler hypothesized that personal characteristics can influence leader effectiveness. He used the term *leader style* to refer to a manager’s characteristic approach to leadership and identified two basic leader styles: relationship-oriented and task-oriented. All managers can be described as having one style or the other.

Relationship-oriented leaders are primarily concerned with developing good relationships with their subordinates and being liked by them. Relationship-oriented managers focus on having high-quality interpersonal relationships with subordinates. This does not mean, however, that the job does not get done when relationship-oriented leaders are at the helm. But it does mean that the quality of interpersonal relationships with subordinates is a prime concern for relationship-oriented leaders. Lawrence Fish, for example, is the chairman of Citizens Financial Group Inc. of

relationship-oriented leaders

Leaders whose primary concern is to develop good relationships with their subordinates and to be liked by them.

Providence, Rhode Island, which has tripled its assets in the last three years. As the top manager who helped to engineer this rapid growth, Fish has never lost sight of the importance of good relationships and personally writes a thank-you note to at least one of his subordinates each day.³³

task-oriented leaders Leaders whose primary concern is to ensure that subordinates perform at a high level.

Task-oriented leaders are primarily concerned with ensuring that subordinates perform at a high level. Task-oriented managers focus on task accomplishment and making sure the job gets done. Some task-oriented leaders, like the top managers of the family-owned C. R. England Refrigerated Trucking Company based in Salt Lake City, Utah, go so far as to closely measure and evaluate performance on a weekly basis to ensure subordinates are performing as well as they can.³⁴

SITUATIONAL CHARACTERISTICS According to Fiedler, leadership style is an enduring characteristic; managers cannot change their style, nor can they adopt different styles in different kinds of situations. With this in mind, Fiedler identified three situational characteristics that are important determinants of how favorable a situation is for leading: leader-member relations, task structure, and position power. When a situation is favorable for leading, it is relatively easy for a manager to influence subordinates so that they perform at a high level and contribute to organizational efficiency and effectiveness. In a situation unfavorable for leading, it is much more difficult for a manager to exert influence.

LEADER-MEMBER RELATIONS The first situational characteristic that Fiedler described, **leader-member relations**, is the extent to which followers like, trust, and are loyal to their leader. Situations are more favorable for leading when leader-member relations are good.

leader-member relations The extent to which followers like, trust, and are loyal to their leader; a determinant of how favorable a situation is for leading.

TASK STRUCTURE The second situational characteristic that Fiedler described, **task structure**, is the extent to which the work to be performed is clear-cut so that a leader's subordinates know what needs to be accomplished and how to go about doing it. When task structure is high, the situation is favorable for leading. When task structure is low, goals may be vague, subordinates may be unsure of what they should be doing or how they should do it, and the situation is unfavorable for leading.

task structure The extent to which the work to be performed is clear-cut so that a leader's subordinates know what needs to be accomplished and how to go about doing it; a determinant of how favorable a situation is for leading.

Task structure was low for Geraldine Laybourne when she was a top manager at Nickelodeon, the children's television network. It was never precisely clear what would appeal to her young viewers, whose tastes can change dramatically, or how to motivate her subordinates to come up with creative and novel ideas.³⁵ In contrast, Herman Mashaba, founder and owner of Black Like Me, a hair care products company based in South Africa, seems to have relatively high task structure in his leadership situation. His company's goals are to produce and sell inexpensive hair care products to native Africans, and managers accomplish these goals by using simple yet appealing packaging and distributing the products through neighborhood beauty salons.³⁶

position power The amount of legitimate, reward, and coercive power that a leader has by virtue of his or her position in an organization; a determinant of how favorable a situation is for leading.

POSITION POWER The third situational characteristic that Fiedler described, **position power**, is the amount of legitimate reward and coercive power a leader has by virtue of his or her position in an organization. Leadership situations are more favorable for leading when position power is strong.

COMBINING LEADER STYLE AND THE SITUATION By taking all possible combinations of good and poor leader-member relations, high and low task structure, and strong and weak position power, Fiedler identified eight leadership situations, which vary in their favorability for leading (see Figure 10.2). After

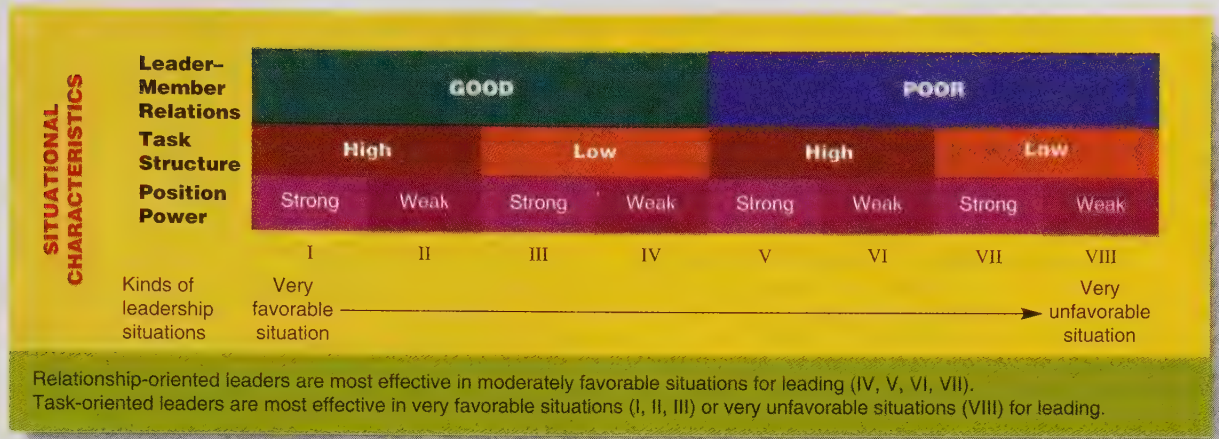


Figure 10.2

Fiedler's Contingency Theory of Leadership

extensive research, he determined that relationship-oriented leaders are most effective in moderately favorable situations (situations IV, V, VI, and VII in Figure 10.2) and task-oriented leaders are most effective in very favorable (situations I, II, and III) or very unfavorable situations (situation VIII).

PUTTING THE CONTINGENCY MODEL INTO PRACTICE Recall that, according to Fiedler, leader style is an enduring characteristic that managers cannot change. This suggests that to be effective, either managers need to be placed in leadership situations that fit their style or situations need to be changed to suit the managers. Situations can be changed, for example, by giving a manager more position power or taking steps to increase task structure, such as by clarifying goals.

Take the case of Mark Compton, a relationship-oriented leader employed by a small construction company, who was in a very unfavorable situation and having a rough time leading his construction crew. His subordinates did not trust him to look out for their well-being (poor leader-member relations); the construction jobs he supervised tended to be novel and complex (low task structure); and he had no control over the rewards and disciplinary actions his subordinates received (weak position power). Recognizing the need to improve matters, Compton's supervisor gave him the power to reward crew members with bonuses and overtime work as he saw fit and to discipline crew members for poor-quality work and unsafe on-the-job behavior. As his leadership situation improved to moderately favorable, so too did Compton's effectiveness as a leader and the performance of his crew.

Research studies tend to support some aspects of Fiedler's model but also suggest that, like most theories, it needs some modifications.³⁷ Some researchers have questioned what the LPC scale really measures. Others find fault with the model's premise that leaders cannot alter their styles. That is, it is likely that at least some leaders can diagnose the situation they are in and, when their style is inappropriate for the situation, modify their style so that it is more in line with what the leadership situation calls for.

House's path-goal theory

In what he called **path-goal theory**, leadership researcher Robert House focused on what leaders can do to motivate their subordinates to achieve group and

path-goal theory A contingency model of leadership proposing that leaders can motivate subordinates by identifying their desired outcomes, rewarding them for high performance and the attainment of work goals with these desired outcomes, and clarifying for them the paths leading to the attainment of work goals.

organizational goals.³⁸ The premise of path-goal theory is that effective leaders motivate subordinates to achieve goals by (1) clearly identifying the outcomes that subordinates are trying to obtain from the workplace, (2) rewarding subordinates with these outcomes for high performance and the attainment of work goals, and (3) clarifying for subordinates the *paths* leading to the attainment of work *goals*. Path-goal theory is a contingency model because it proposes that the steps managers should take to motivate subordinates depend on both the nature of the subordinates and the type of work they do.

Path-goal theory identifies four kinds of leadership behaviors that motivate subordinates:

- *Directive behaviors* are similar to initiating structure and include setting goals, assigning tasks, showing subordinates how to complete tasks, and taking concrete steps to improve performance.
- *Supportive behaviors* are similar to consideration and include expressing concern for subordinates and looking out for their best interests.
- *Participative behaviors* give subordinates a say in matters and decisions that affect them.
- *Achievement-oriented behaviors* motivate subordinates to perform at the highest level possible by, for example, setting very challenging goals, expecting that they be met, and believing in subordinates' capabilities.

Which of these behaviors should managers use to lead effectively? The answer to this question depends, or is contingent on, the nature of the subordinates and the kind of work they do.

Directive behaviors may be beneficial when subordinates are having difficulty completing assigned tasks, but they might be detrimental when subordinates are independent thinkers who work best when left alone. *Supportive* behaviors are often advisable when subordinates are experiencing high levels of stress. *Participative* behaviors can be particularly effective when subordinates' support of a decision is required. *Achievement-oriented* behaviors may increase motivation levels of highly capable subordinates who are bored from having too few challenges, but they might backfire if used with subordinates who are already pushed to their limit.

Effective managers seem to have a knack for determining what kinds of leader behaviors are likely to work in different situations and result in increased effectiveness, as indicated in the following "Management Insight."



Management Insight

Supporting Creativity

What do playing in an orchestra and designing high-status automobiles have in common? Both activities require creativity from artistic individuals. Effectively leading workers who are engaged in creative activities can be a challenge. For example, too much initiating structure can inhibit their creativity. Roger Nierenberg, conductor of the Stamford, Connecticut, Symphony Orchestra has long recognized this, and rather than being overly controlling with musicians, he emphasizes supportive behaviors. Nierenberg utilizes positive feedback to support his musicians, never blames them when things go wrong, and provides direction in an encouraging manner.³⁹



A positive, encouraging style of leadership often gets the best results from creative employees—whether they are musicians or automobile designers.

Nierenberg's positive, encouraging style of leading and conducting also can be applied in more traditional work environments. For example, in his leadership classes for managers at major corporations, such as Lucent Technologies and Georgia-Pacific, he coaches the managers on how to commit to a course of action and direct their subordinates to attain it in a supportive, uncritical manner.⁴⁰

This approach to leading creative workers is applied in other countries as well. For example, Chris Bangle, who heads BMW's global design efforts in Munich, Germany, takes great pains to shield creative designers of BMW interiors and exteriors from critical comments or negative feedback from others in the organization, such as market analysts and engineers. Rather than receiving critiques, designers need, above all else, support from leadership and

the freedom to explore different designs, as well as to encourage direction to reach closure in a reasonably timely fashion.⁴¹ Bangle sees this kind of encouraging and supportive leadership as key to BMW's competitive advantage in designing cars like "moving works of art that express the driver's love of quality."⁴²

The leader substitutes model

The leader substitutes model suggests that leadership is sometimes unnecessary because substitutes for leadership are present. A **leadership substitute** is something that acts in place of the influence of a leader and makes leadership unnecessary. This model suggests that under certain conditions managers do not have to play a leadership role—that members of an organization sometimes can perform highly without a manager exerting influence over them.⁴³ The leader substitutes model is a contingency model because it suggests that in some situations leadership is unnecessary.

Take the case of David Cotsonas, who teaches English at a foreign-language school in Cyprus, an island in the Mediterranean Sea. Cotsonas is fluent in Greek, English, and French, is an excellent teacher, and is highly motivated. Many of his students are businesspeople who have some rudimentary English skills and wish to increase their fluency to be able to conduct more of their business in English. He enjoys not only teaching them English but also learning about the work they do, and he often keeps in touch with his students after they finish his classes. Cotsonas meets with the director of the school twice a year to discuss semiannual class schedules and enrollments.

With practically no influence from a leader, Cotsonas is a highly motivated top performer at the school. In his situation, leadership is unnecessary because substitutes for leadership are present. Cotsonas's teaching expertise, his motivation, and his enjoyment of his work all are substitutes for the influence of a leader—in this case, the school's director. If the school's director were to try to exert influence over the way Cotsonas goes about performing his job, Cotsonas would probably resent this infringement on his autonomy, and it is unlikely that his performance would improve because he is already one of the school's best teachers.

As in Cotsonas's case, *characteristics of subordinates*—such as their skills, abilities, experience, knowledge, and motivation—can be substitutes for leadership.⁴⁴ *Characteristics*

leadership substitute A characteristic of a subordinate or characteristic of a situation or context that acts in place of the influence of a leader and makes leadership unnecessary.

of the situation or context—such as the extent to which the work is interesting and enjoyable—also can be substitutes. When work is interesting and enjoyable, as it is for Cotsonas, jobholders do not need to be coaxed into performing because performing is rewarding in its own right. Similarly, when managers *empower* their subordinates or use *self-managed work teams* (discussed in detail in Chapter 11), the need for leadership influence from a manager is decreased because team members manage themselves.

Substitutes for leadership can increase organizational efficiency and effectiveness because they free up some of managers' valuable time and allow managers to focus their efforts on discovering new ways to improve organizational effectiveness. The director of the language school, for example, was able to spend much of his time making arrangements to open a second school in Rhodes, an island in the Aegean Sea, because of the presence of leadership substitutes, not only in the case of Cotsonas but for most of the other teachers at the school as well.

Bringing it all together

Effective leadership in organizations occurs when managers take steps to lead in a way that is appropriate for the situation or context in which leadership occurs and for the subordinates who are being led. The three contingency models of leadership discussed above help managers home in on the necessary ingredients for effective leadership. They are complementary in that each one looks at the leadership question from a different angle. Fiedler's contingency model explores how a manager's leadership style needs to be matched to that person's leadership situation for maximum effectiveness. House's path-goal theory focuses on how managers should motivate subordinates and describes the specific kinds of behaviors that managers can engage in to have a highly motivated workforce. The leadership substitutes model alerts managers to the fact that sometimes they do not need to exert influence over subordinates and thus can free up their time for other important activities. Table 10.2 recaps these three contingency models of leadership.

Table 10.2
Contingency Models of Leadership

Model	Focus	Key Contingencies
Fiedler's Contingency Model	Describes two leader styles, relationship-oriented and task-oriented, and the kinds of situations in which each kind of leader will be most effective	Whether or not a relationship-oriented or a task-oriented leader is effective is contingent on the situation
House's Path-Goal Theory	Describes how effective leaders motivate their followers	The behaviors that managers should engage in to be effective leaders are contingent on the nature of the subordinates and the work they do
Leader Substitutes Model	Describes when leadership is unnecessary	Whether or not leadership is necessary for subordinates to perform highly is contingent on characteristics of the subordinates and the situation

Transformational Leadership

Time and time again, throughout business history, certain leaders seem to literally transform their organizations, making sweeping changes to revitalize and renew operations. For example, in the 1990s, the chief executive of the

German electronics company Siemens, Heinrich von Pierer, dramatically transformed his company. When von Pierer took over in 1992, Siemens had a rigid hierarchy in place, was suffering from increased global competition, and was saddled with a conservative, perfectionist culture that stifled creativity and innovation and slowed decision making. Von Pierer's changes at Siemens were nothing short of revolutionary.⁴⁵ At the new Siemens, subordinates critique their managers, who receive training in how to be more democratic and participative and spur creativity. Employees are no longer afraid to speak their minds, and the quest for innovation is a driving force throughout the company.

Von Pierer literally transformed Siemens and its thousands of employees into being more innovative and taking the steps needed to gain a competitive advantage. When managers have such dramatic effects on their subordinates and on an organization as a whole, they are engaging in transformational leadership. **Transformational leadership** occurs when managers change (or transform) their subordinates in the following three important ways.⁴⁶

transformational leadership

Leadership that makes subordinates aware of the importance of their jobs and performance to the organization and aware of their own needs for personal growth and that motivates subordinates to work for the good of the organization.

1. *Transformational managers make subordinates aware of how important their jobs are for the organization and how necessary it is for them to perform those jobs as best they can so that the organization can attain its goals.* Von Pierer sent the message throughout Siemens not only that innovating, cost cutting, and increasing customer service and satisfaction were everyone's responsibilities but also that improvements could be and needed to be made in these areas. For example, when von Pierer realized that managers in charge of microprocessor sales were not aware of the importance of their jobs and of performing them in a top-notch fashion, he had managers from Siemens's top microprocessor customers give the Siemens's microprocessor managers feedback about their poor service and unreliable delivery schedules. The microprocessor managers quickly realized how important it was for them to take steps to improve customer service.
2. *Transformational managers make their subordinates aware of the subordinates' own needs for personal growth, development, and accomplishment.* Von Pierer has made Siemens's employees aware of their own needs in this regard through numerous workshops and training sessions, through empowering employees throughout the company, through the development of fast-track career programs, and through increased reliance on self-managed work teams.⁴⁷
3. *Transformational managers motivate their subordinates to work for the good of the organization as a whole, not just for their own personal gain or benefit.* Von Pierer's message to Siemens's employees was clear: Dramatic changes in the way they perform their jobs were crucial for the future viability and success of Siemens. As von Pierer put it, "We have to keep asking ourselves: Are we flexible enough? Are we changing enough?"⁴⁸ One way von Pierer tried to get all employees thinking in these terms was by inserting in the company magazine distributed to all employees self-addressed postcards urging them to send in their ideas for making improvements to him directly.

When managers transform their subordinates in these three ways, subordinates trust the manager, are highly motivated, and help the organization achieve its goals. As a result of von Pierer's transformational leadership, for example, a team of

Table 10.3
Transformational Leadership

Transformational Managers

- Are charismatic
- Intellectually stimulate subordinates
- Engage in developmental consideration

Subordinates of Transformational Managers

- Have increased awareness of the importance of their jobs and high performance
- Are aware of their own needs for growth, development, and accomplishment
- Work for the good of the organization and not just their own personal benefit

Siemens's engineers working in blue jeans in a rented house developed a tool control system in one-third the time and at one-third the cost of other similar systems developed at Siemens.⁴⁹ How do managers like von Pierer transform subordinates and produce dramatic effects in their organizations? There are at least three ways in which managers and other transformational leaders can influence their followers: by being a charismatic leader, by stimulating subordinates intellectually, and by engaging in developmental consideration (see Table 10.3).

Being a charismatic leader

charismatic leader

An enthusiastic, self-confident leader who is able to clearly communicate his or her vision of how good things could be.

Transformational managers are **charismatic leaders**. They have a vision of how good things could be in their work groups and organizations that is in contrast with the status quo. Their vision usually entails dramatic improvements in group and organizational performance as a result of changes in the organization's structure, culture, strategy, decision making, and other critical processes and factors. This vision paves the way for gaining a competitive advantage.

Charismatic leaders are excited and enthusiastic about their vision and clearly communicate it to their subordinates. The excitement, enthusiasm, and self-confidence of a charismatic leader contribute to the leader's being able to inspire followers to enthusiastically support his or her vision.⁵⁰ People often think of charismatic leaders or managers as being "larger than life." The essence of charisma, however, is having a vision and enthusiastically communicating it to others. Thus, managers who appear to be quiet and earnest can also be charismatic.

Stimulating subordinates intellectually

intellectual stimulation

Behavior a leader engages in to make followers be aware of problems and view these problems in new ways, consistent with the leader's vision.

Transformational managers openly share information with their subordinates so that they are aware of problems and the need for change. The manager causes subordinates to view problems in their groups and throughout the organization from a different perspective, consistent with the manager's vision. Whereas in the past subordinates might not have been aware of some problems, may have viewed problems as a "management issue" beyond their concern, or may have viewed problems as insurmountable, the transformational manager's **intellectual stimulation** leads subordinates to view problems as challenges that they can and will meet and conquer. The manager engages and empowers subordinates to take personal responsibility for helping solve problems.⁵¹

developmental consideration

Behavior a leader engages in to support and encourage followers and help them develop and grow on the job.

Engaging in developmental consideration

When managers engage in **developmental consideration**, they not only perform the consideration behaviors described earlier, such as demonstrating true concern for the well-being of subordinates, but go one step further. The manager goes out of his or her way to support and encourage subordinates, giving them opportunities to enhance their skills and capabilities and to grow and excel on the job.⁵² Heinrich von Pierer engaged in developmental consideration in numerous ways, such as by providing counseling sessions with a psychologist for managers who were having a hard time adapting to the changes at Siemens and sponsoring hiking trips to stimulate employees to think and work in new ways.⁵³

All organizations, no matter how large or small, successful or unsuccessful, can benefit when their managers engage in transformational leadership. Moreover, while the benefits of transformational leadership are often most apparent when an organization is in trouble, transformational leadership can be an enduring approach to leadership, leading to long-run organizational effectiveness.

The distinction between transformational and transactional leadership

transactional leadership

Leadership that motivates subordinates by rewarding them for high performance and reprimanding them for low performance.

Transformational leadership is often contrasted with transactional leadership. In **transactional leadership**, managers use their reward and coercive powers to encourage high performance. When managers reward high performers, reprimand or otherwise punish low performers, and motivate subordinates by reinforcing desired behaviors and extinguishing or punishing undesired ones, they are engaging in transactional leadership.⁵⁴ Managers who effectively influence their subordinates to achieve goals yet do not seem to be making the kind of dramatic changes that are part of transformational leadership are engaging in transactional leadership.

Many transformational leaders engage in transactional leadership. They reward subordinates for a job well done and notice and respond to substandard performance. But they also have their eyes on the bigger picture of how much better things could be in their organizations, how much more their subordinates are capable of achieving, and how important it is to treat their subordinates with respect and to help them reach their full potential.

Research has found that when leaders engage in transformational leadership, their subordinates tend to have higher levels of job satisfaction and performance.⁵⁵ Additionally, subordinates of transformational leaders may be more likely to trust their leaders and their organizations and feel that they are being fairly treated, and this, in turn, may positively influence their work motivation (see Chapter 9).⁵⁶

Gender and Leadership

The increasing number of women entering the ranks of management, as well as the problems some women face in their efforts to be hired as managers or promoted into management positions, has prompted researchers to explore the relationship between gender and leadership. Although there are relatively more women in management positions today than there were 10 years ago, there are still relatively few women in top management and, in some organizations, even in middle management.

When women do advance to top-management positions, special attention often is focused on them and the fact that they are women. For example, women CEOs of large companies are still very rare; those who make it to the very top post, such as Meg Whitman of eBay and Andrea Jung of Avon, are very salient. As business writer Linda Tischler puts it, "In a workplace where women CEOs of major companies are so scarce . . . they can be identified, like rock stars, by first name only—Andrea and Oprah and Meg."⁵⁷ While women have certainly made inroads into leadership positions in organizations, they continue to be very underrepresented in top leadership posts (see Chapter 3). For example, it is estimated that the percentage of women in top leadership/partner positions in law firms is less than 16 percent. Less than 7 percent of the top-earning medical doctors are women, and of the corporate officers of the Fortune 500 largest U.S. companies, less than 16 percent are women.⁵⁸

A widespread stereotype of women is that they are nurturing, supportive, and concerned with interpersonal relations. Men are stereotypically viewed as being directive and focused on task accomplishment. Such stereotypes suggest that women tend to be more relationship-oriented as managers and engage in more consideration behaviors, whereas men are more task-oriented and engage in more initiating-structure behaviors. Does the behavior of actual male and female managers bear out these stereotypes? Do women managers lead in different ways than men? Are male or female managers more effective as leaders?

Research suggests that male and female managers who have leadership positions in organizations behave in similar ways.⁵⁹ Women do not engage in more consideration than men, and men do not engage in more initiating structure than women. Research does suggest, however, that leadership style may vary between women and men. Women tend to be somewhat more participative as leaders than are men, involving subordinates in decision making and seeking their input.⁶⁰ Male managers tend to be less participative than are female managers, making more decisions on their own and wanting to do things their own way. Moreover, research suggests that men tend to be harsher when they punish their subordinates than are women.⁶¹

There are at least two reasons why female managers may be more participative as leaders than are male managers.⁶² First, subordinates may try to resist the influence of female managers more than they do the influence of male managers. Some subordinates may never have reported to a woman before; some may incorrectly see a management role as being more appropriate for a man than for a woman; and some may just resist being led by a woman. To overcome this resistance and encourage subordinates' trust and respect, women managers may adopt a participative approach.

A second reason why female managers may be more participative is that they sometimes have better interpersonal skills than male managers.⁶³ A participative approach to leadership requires high levels of interaction and involvement between a manager and his or her subordinates, sensitivity to subordinates' feelings, and the ability to make decisions that may be unpopular with subordinates but necessary for goal attainment. Good interpersonal skills may help female managers have the effective interactions with their subordinates that are crucial to a participative approach.⁶⁴ To the extent that male managers have more difficulty managing interpersonal relationships, they may shy away from the high levels of interaction with subordinates necessary for true participation.

The key finding from research on leader behaviors, however, is that male and female managers do *not* differ significantly in their propensities to perform different leader behaviors. Even though they may be more participative, female managers do not engage in more consideration or less initiating structure than male managers.

Perhaps a question even more important than whether male and female managers differ in the leadership behaviors they perform is whether they differ in effectiveness. Consistent with the findings for leader behaviors, research suggests that across different kinds of organizational settings, male and female managers tend to be *equally effective* as leaders.⁶⁵ Thus, there is no logical basis for stereotypes favoring male managers and leaders or for the existence of the “glass ceiling” (an invisible barrier that seems to prevent women from advancing as far as they should in some organizations). Because women and men are equally effective as leaders, the increasing number of women in the workforce should result in a larger pool of highly qualified candidates for management positions in organizations, ultimately enhancing organizational effectiveness.⁶⁶

An important factor for women’s advancement to top leadership positions is obtaining a variety of work experiences.⁶⁷ Varied work experiences have proved very beneficial for Kathleen Ligocki, CEO and president of Tower Automotive, Inc., as profiled in the following “Focus on Diversity.”

Focus on Diversity

Kathleen Ligocki Leads Tower Automotive

Kathleen Ligocki occupies perhaps one of the highest leadership positions held by a woman in the automotive industry. As CEO and a director of Tower Automotive, Ligocki leads an automobile components and assemblies firm that supplies car parts to every major automaker, has approximately \$2.8 billion in sales, and operates in 13 countries in addition to the United States, ranging from Mexico, Germany, and Japan to Poland, Slovakia, Brazil, and India.⁶⁸



Tower Automotive CEO Kathleen Ligocki draws on her prior experience in various positions at Ford in transforming her company.

With a BA in Chinese history and Renaissance art from Indiana University, Ligocki had no plans for a career in the automotive industry.⁶⁹ Upon receiving her undergraduate degree, she took a job as a foreman in a General Motors (GM) factory to earn money for graduate school. Much to her surprise, she realized she loved her work and went on to a number of different positions at GM and later at the Ford Motor Company; along the way, she also earned a master’s degree from the Wharton Business School.⁷⁰ Ligocki’s positions at Ford included

director of strategies, CEO of Ford Mexico, and, most recently, vice president of Ford's Customer Service Division.⁷¹

Bill Ford was so impressed with Ligocki's leadership capabilities that he remarked just weeks before she accepted the Tower top post that she might someday be the one to lead Ford. In fact, when she discussed potentially leaving Ford to become CEO of Tower with Ford top managers, they tried to convince her to stay but also appreciated the kind of opportunity she would have at Tower. As Ligocki put it, "They encouraged me to stay, but they also understood—maybe Bill better than anybody—that this was an opportunity to run a publicly traded company. . . . Tower . . . was a company I thought had great strategic strengths. . . . But it needed operational work, which was a lot of what I had done at GM and Ford. So I felt I could offer something to the company."⁷²

Varied work experiences in both line and administrative positions have paid off for Ligocki in terms of having a very motivating and rewarding career and being especially well suited for her current leadership position. In less than a few years in her current position, which she assumed in August 2003, she has already begun to transform Tower, diversifying both its corporate customers and the countries it operates in. Under Ligocki's leadership, Tower projects that its annual revenues in 2006 will be over \$3.3 billion.⁷³

Emotional Intelligence and Leadership

Do the moods and emotions leaders experience on the job influence their behavior and effectiveness as leaders? Preliminary research suggests that this is likely to be the case. For example, one study found that when store managers experienced positive moods at work, salespeople in their stores provided high-quality customer service and were less likely to quit.⁷⁴

Moreover, a leader's level of emotional intelligence (see Chapter 2) may play a particularly important role in leadership effectiveness.⁷⁵ For example, emotional intelligence may help leaders develop a vision for their organizations, motivate their subordinates to commit to this vision, and energize them to enthusiastically work to achieve this vision. Moreover, emotional intelligence may enable leaders to develop a significant identity for their organization and instill high levels of trust and cooperation throughout the organization while maintaining the flexibility needed to respond to changing conditions.⁷⁶

Emotional intelligence also plays a crucial role in how leaders relate to and deal with their followers, particularly when it comes to encouraging followers to be creative.⁷⁷ Creativity in organizations is an emotion-laden process, as it often entails challenging the status quo, being willing to take risks and accept and learn from failures, and doing much hard work to bring creative ideas to fruition in terms of new products, services, or procedures and processes when uncertainty is bound to be high.⁷⁸ Leaders who are high on emotional intelligence are more likely to understand all the emotions surrounding creative endeavors, to be able to awaken and support the creative pursuits of their followers, and to provide the kind of support that enables creativity to flourish in organizations.⁷⁹

Summary and Review

THE NATURE OF LEADERSHIP Leadership is the process by which a person exerts influence over other people and inspires, motivates, and directs their activities to help achieve group or organizational goals. Leaders

are able to influence others because they possess power. The five types of power available to managers are legitimate power, reward power, coercive power, expert power, and referent power. Many managers are using empowerment as a tool to increase their effectiveness as leaders.

TRAIT AND BEHAVIOR MODELS OF LEADERSHIP The trait model of leadership describes personal characteristics or traits that contribute to effective leadership. However, some managers who possess these traits are not effective leaders, and some managers who do not possess all the traits are nevertheless effective leaders. The behavior model of leadership describes two kinds of behavior that most leaders engage in: consideration and initiating structure.

CONTINGENCY MODELS OF LEADERSHIP Contingency models take into account the complexity surrounding leadership and the role of the situation in determining whether a manager is an effective or ineffective leader. Fiedler's contingency model explains why managers may be effective leaders in one situation and ineffective in another. According to Fiedler's model, relationship-oriented leaders are most effective in situations that are moderately favorable for leading, and task-oriented leaders are most effective in situations that are very favorable or very unfavorable for leading. House's path-goal theory describes how effective managers motivate their subordinates by determining what outcomes their subordinates want, rewarding subordinates with these outcomes when they achieve their goals and perform at a high level, and clarifying the paths to goal attainment. Managers can engage in four different kinds of behaviors to motivate subordinates: directive behaviors, supportive behaviors, participative behaviors, and achievement-oriented behaviors. The leader substitutes model suggests that sometimes managers do not have to play a leadership role because their subordinates perform highly without the manager having to exert influence over them.

TRANSFORMATIONAL LEADERSHIP Transformational leadership occurs when managers have dramatic effects on their subordinates and on the organization as a whole and inspire and energize subordinates to solve problems and improve performance. These effects include making subordinates aware of the importance of their own jobs and high performance, making subordinates aware of their own needs for personal growth, development, and accomplishment, and motivating subordinates to work for the good of the organization and not just their own personal gain. Managers can engage in transformational leadership by being charismatic leaders, by intellectually stimulating subordinates, and by engaging in developmental consideration. Transformational managers also often engage in transactional leadership by using their reward and coercive powers to encourage high performance.

GENDER AND LEADERSHIP Female and male managers do not differ in the leadership behaviors that they perform, contrary to stereotypes suggesting

that women are more relationship-oriented and men more task-oriented. Female managers sometimes are more participative than male managers, however. Research has found that women and men are equally effective as managers and leaders.

EMOTIONAL INTELLIGENCE AND LEADERSHIP The moods and emotions leaders experience on the job, and their ability to effectively manage these feelings, can influence their effectiveness as leaders. Moreover, emotional intelligence has the potential to contribute to leadership effectiveness in multiple ways, including encouraging and supporting creativity among followers.



Management in Action

Topics for Discussion and Action

Discussion

1. Describe the steps managers can take to increase their power and ability to be effective leaders.
2. Think of specific situations in which it might be especially important for a manager to engage in consideration and in initiating structure.
3. Discuss why managers might want to change the behaviors they engage in, given their situation, their subordinates, and the nature of the work being done. Do you think managers are able to readily change their leadership behaviors? Why or why not?
4. Discuss why substitutes for leadership can contribute to organizational effectiveness.
5. Describe what transformational leadership is and explain how managers can engage in it.
6. Imagine that you are working in an organization in an entry-level position after graduation and have come up with what you think is a great idea for improving a critical process in the organization that relates to your job. In what ways might your supervisor encourage you to actually implement your idea? How might your supervisor discourage you from even sharing your idea with others?

Action

7. Interview a manager to find out how the three situational characteristics that Fiedler identified are affecting his or her ability to provide leadership.
8. Find a company that has dramatically turned around its fortunes and improved its performance. Determine whether a transformational manager was behind the turnaround and, if one was, what this manager did.

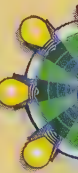


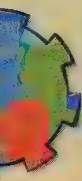
Building Management Skills

Analyzing Failures of Leadership

Think about a situation you are familiar with in which a leader was very ineffective. Then answer the following questions:

1. What sources of power did this leader have? Did the leader have enough power to influence his or her followers?
2. What kinds of behaviors did this leader engage in? Were they appropriate for the situation? Why or why not?
3. From what you know, do you think this leader was a task-oriented leader or a relationship-oriented leader? How favorable was this leader's situation for leading?
4. What steps did this leader take to motivate his or her followers? Were these steps appropriate or inappropriate? Why?
5. What signs, if any, did this leader show of being a transformational leader?





Small Group Breakout Exercise

Improving Leadership Effectiveness

Form groups of three to five people, and appoint one member as the spokesperson who will communicate your findings and conclusions to the whole class when called on by the instructor. Then discuss the following scenario.

You are a team of human resource consultants who have been hired by Carla Caruso, an entrepreneur who has started her own interior decorating business. A highly competent and creative interior decorator, Caruso established a working relationship with most of the major home builders in her community. At first, she worked on her own as an independent contractor. Then, because of a dramatic increase in the number of new homes being built, she became swamped with requests for her services and decided to start her own company.

She hired a secretary-bookkeeper and four interior decorators, all of whom are highly competent. Caruso still does decorating jobs herself and has adopted a hands-off approach to leading the four decorators who report to her because she feels that interior design is a very personal, creative endeavor. Rather than pay the deco-

rators on some kind of commission basis (such as a percentage of their customers' total billings), she pays them a premium salary, higher than average, so that they are motivated to do what's best for a customer's needs and not what will result in higher billings and commissions.

Caruso thought everything was going smoothly until customer complaints started coming in. The complaints ranged from the decorators' being hard to get hold of, promising unrealistic delivery times, and being late for or failing to keep appointments to their being impatient and rude when customers had trouble making up their minds. Caruso knows that her decorators are very competent and is concerned that she is not effectively leading and managing them. She wonders, in particular, if her hands-off approach is to blame and if she should change the manner in which she rewards or pays her decorators. She has asked for your advice.

1. Analyze the sources of power that Caruso has available to her to influence the decorators. What advice can you give her to either increase her power base or use her existing power more effectively?
2. Given what you have learned in this chapter (for example, from the behavior model and path-goal theory), does Caruso seem to be performing appropriate leader behaviors in this situation? What advice can you give her about the kinds of behaviors she should perform?
3. What steps would you advise Caruso to take to increase the decorators' motivation to deliver high-quality customer service?
4. Would you advise Caruso to try to engage in transformational leadership in this situation? If not, why not? If so, what steps would you advise her to take?



Be the Manager

You are the CEO of a medium-size company that makes window coverings such as Hunter Douglas blinds and Douettes. Your company has a real cost advantage in terms of being able to make custom window coverings at costs that are relatively low in the industry. However, the performance of your company has been lackluster. In order to make needed changes and improve performance, you met with the eight other top managers in your company and charged them with

identifying problems and missed opportunities in each of their areas and coming up with an action plan to address the problems and take advantage of opportunities.

Once you gave the managers the okay, they were charged with implementing their action plans in a timely fashion and monitoring the effects of their initiatives on a monthly basis for the next 8 to 12 months.

You approved each manager's action plan, and a year later most of

the managers were reporting that their initiatives had been successful in addressing the problems and opportunities they had identified a year ago. However, overall company performance continues to be lackluster and shows no signs of improvement. You are confused and starting to question your leadership capabilities and approach to change. What are you going to do to improve the performance and effectiveness of your company?

Additional Activities on the Build Your Management Skills DVD

- **Test Your Knowledge:**

- (1) Sources of Power,
- (2) Path-Goal Theory, and
- (3) Fiedler's Contingency Model of Leadership

- **Self-Assessment:**

- (1) Assessing Your Leader-Member Exchange and
- (2) Do You Have What It Takes to Be a Leader?

Managing Ethically

Managers who verbally criticize their subordinates, put them down in front of their co-workers, or use the threat of job loss to influence behavior are exercising coercive power. Some employees subjected to coercive power believe that using it is unethical.

Questions

1. Either alone or in a group, think about the ethical implications of the use of coercive power.
2. To what extent do managers and organizations have an ethical obligation to put limits on the amount of coercive power that is exercised?

BusinessWeek

Case in the News

Siemens' New Boss: Can He Deliver?

Workers at a Siemens unit that makes X-ray machines and other diagnostic equipment were shocked when, in 1998, a cocky new boss asked them to work more flexible shifts to speed production. The new guy, a 40-year-old up-and-comer named Klaus Kleinfeld, even wanted weekend shifts, then practically unheard of. Yet employee representatives knew the unit in Forchheim, Bavaria, was getting beat up by General Electric Co., and that shareholders wanted Siemens to dump its medical equipment unit. Everyone's job was on the line.

The negotiations were tough. But Kleinfeld won over workers, hanging around the factory asking detailed questions. He answered e-mails from employee reps almost immediately, even late at night, recalls Werner Mönius, chairman of the worker's council in Erlangen, Germany, home base of Siemens Medical Solutions. "He was able to

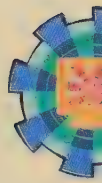
motivate people to pull together," says Mönius. The workers signed off on Kleinfeld's plan, which helped cut the time it took to build a \$100,000-plus diagnostic scanner from six weeks to one. Siemens Medical Solutions Div. is now Siemens' most profitable business.

And that cocky young boss? This month Kleinfeld, now 47, becomes chief executive of Munich-based Siemens, a \$100 billion behemoth that operates in 190 countries and makes subways, light bulbs, power plants, auto parts, automatic mail-sorting gear, and more. With 430,000 employees and 12 major divisions, Siemens is the rock of Germany Inc., which still needs to learn how to survive and thrive in a world where heavily taxed, slow-moving European companies operate at a disadvantage. If Siemens can reach new levels of profitability, maybe the rest of Corporate Germany has a chance, too.

Opera Man

Siemens Chief Executive Heinrich von Pierer and the company's supervisory board skipped over more seasoned top managers to choose the ferociously energetic Kleinfeld. He represents a new breed of German manager, fluent in English and comfortable in settings from Tokyo to Toledo. With his big laugh and knack for storytelling, Kleinfeld knows how to network globally as well. He sits on several corporate and charitable boards abroad, including those of aluminum-products maker Alcoa and the Metropolitan Opera in New York. "I love him. He's a generous, funny man," says Beverly Sills, chairman of the Met, who gushes about Kleinfeld's ability to appraise opera performances.

Kleinfeld should not let such praise go to his head. His swift rise and role as an internal consultant at Siemens, which had him



parachuting in to fix troubled businesses, inevitably bred resentment in some quarters. And it will take Kleinfeld years to match the stature of von Pierer, now something of a national hero after steering Siemens through an age of rapid globalization. If Kleinfeld pushes for change too hard, he will face resistance from all quarters.

If nothing else, Kleinfeld should help put to rest stereotypes about dour German execs. At a November dinner in Munich with business journalists, one Italian scribe waved his Nokia mobile phone in Kleinfeld's face and demanded to know how Siemens can compete with the handset industry's market leader. Kleinfeld replied by snatching the Nokia phone and dropping it in a glass of water. The message: We'll drown the competition. (Kleinfeld later gave the journalist a waterproof Siemens phone instead.) But the reporter's question was legitimate. Does Kleinfeld have what it takes to fix Siemens' money-losing mobile-handset business and other underperformers?

On the plus side, he inherits a company that has come far since von Pierer took over in 1992. Since then sales have nearly doubled, to \$98 billion, and profit has more than tripled, to \$4.5 billion, a sum analysts expect to increase by at least 10 percent more in 2005.

Yet Siemens still suffers in comparison with archrival GE, whose shares have had a total return of 423 percent over the last 10 years, versus 273 percent for the German company. It's not just a question of cutting costs. "In the innovation game, productivity and R&D matter more than cost structure," says William M. Castell, CEO of GE Healthcare. Siemens boasts that it generates more than 8,000 inventions a year, but it needs to do more to turn them into profitable prod-

ucts. Siemens must also persuade the market to value it for more than its 12 units would be worth separately. Munich bank HVB Group figures Siemens is worth about \$96 per share based on a sum-of-the-parts valuation. The stock trades around \$80. "You never [see] a great year when all businesses are performing well," says Henning Gebhardt, head of German equities at DWS, a mutual-fund company.

Inside Peeks

Can he succeed? Kleinfeld doubtless has the drive. His father died when the boy was 10—a "brutal" experience, Kleinfeld says. An only child, he stocked grocery shelves at age 12. After studying business at Georg August University in Göttingen, Kleinfeld put in stints at a Nuremberg market research firm and at drugmaker Ciba-Geigy before joining Siemens in 1987. He completed his doctorate at the University of Würzburg while working full time at Siemens and raising a family. "That was an extreme burden," recalls Ulli Arnold, now a business professor at University of Stuttgart, who supervised Kleinfeld's thesis work on corporate identity and strategic management. Kleinfeld's stamina has, if anything, increased. George C. Nolen, CEO of Siemens Corp., the company's U.S. unit, recalls returning from a European trip with Kleinfeld. "I was dead tired, and he runs the New York City marathon," Nolen says.

Kleinfeld has held 10 jobs within Siemens in 17 years, including building up the in-house consulting arm. Under Kleinfeld, it grew from 8 consultants to 170 operating under direct control of the management board, and it was involved in turnarounds of divisions such as power generation. His job-hopping and role as an internal consultant have led to muttering that Kleinfeld is

short on operational experience. But his stint as a consultant has also allowed him to explore every corner of the Siemens empire. He enjoys telling tales of his adventures, such as an all-night session with the glum managers of a troubled Japanese unit. Fatigue and sake loosened their reserve until they worked out a new business plan.

Team Turnaround

Kleinfeld was one of the main inventors of One Siemens, a program designed to promote internal cooperation. He got a chance to put theory into practice when Siemens sent him to the U.S. in January, 2001, first as chief operating officer, and, a year later, as CEO of New York-based Siemens Corp. Under Kleinfeld, units including Medical Solutions and Power Transmission & Distribution teamed up to supply diagnostic gear, software, telecommunications, and power to a hospital being built in Temple, Tex., for Scott & White Healthcare System. It worked: Kleinfeld inherited a roughly \$500 million loss when he arrived in the U.S. When he left, U.S. operations were \$500 million in the black.

Last year his fingerprints were on the choice to merge Siemens' mobile and land-line telecom businesses. But more job cuts may be necessary, and the money-losing handset business may have to merge with a rival. Kleinfeld probably can't take such action without the support of von Pierer, who will stay on as chairman of the supervisory board. But he may get it. Von Pierer has said sale or closure of the handset unit are options.

A whole generation of young Siemens executives, meanwhile, is rooting for Kleinfeld. Robert H. Schaffer, a Stamford (Conn.) consultant who has helped design

training programs for Siemens as well as GE, says mid-level managers at Siemens "are as bright and as aggressive as any I have met." The talent is there. But the task—transforming the prime symbol of Germany Inc.—is huge.

Questions

1. How would you characterize Klaus Kleinfeld's personal leadership style?

2. What leader traits does he appear to possess and what kinds of leader behaviors does he engage in?
3. To what extent does Kleinfeld engage in transformational leadership?

4. How does Kleinfeld motivate employees at Siemens?

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BusinessWeek

Case in the News

The Jack Welch of the Meat Aisle

The first question Lawrence R. Johnston asked when a head-hunter got in touch with him three years ago about running Albertsons Inc. was: "What's Albertsons?" But it didn't take long for Johnston, then the chief executive of GE Appliances and often on the receiving end of such feelers, to realize that Albertsons, the nation's second-largest grocery chain, was the opportunity he had been waiting for. His assignments at General Electric Co., especially resuscitating its ailing European medical services business in the late 1990s, had been so challenging that every other job he considered felt as if he would be taking early retirement. Not so at Albertsons. "This one intrigued me because it was very close to customers. It was big. It was complex. And it was broken," he says.

It certainly was. The folksy, family-owned grocery chain that Joe Albertson started in Boise, Idaho, in 1939 had become a \$35 billion dysfunctional mess. The company had botched the integration of its 1999 merger with American Stores Co. "It was clear we didn't know who we were," recalls Paul I. Corddry, a board member since 1987. And

while executives were preoccupied with union battles and lawsuits, Wal-Mart Stores, Target, and other discount retailers were eating Albertsons for lunch.

"Larry Can Lead"

Johnston, 56, had been a lifer at GE. He joined in 1972 right after graduating from Stetson University in Florida with a degree in business, distinguished himself early on with his salesmanship, took on a series of increasingly high-profile assignments for two decades, and came within reach of Jack Welch's job. That was mostly because of his record at the medical services division. Welch dispatched him to Paris in 1997 to fix the business, which was losing \$100 million a year, or dump it.

In less than three years, the division was making a \$100 million operating profit. According to Welch, Johnston succeeded because he quickly realized his chief task was reenergizing the employees. "This was a cynical group of French and German engineers," Welch recalls. "But he engaged them incredibly." Every month Johnston traveled to a different European city, conducting

sales meetings in the mornings and taking his team to visit hospitals in the afternoons. And at nights he studied French. "Larry can lead people over the hill," Welch says. "He put us on the map in Europe."

So it's safe to say that Johnston came to Albertsons in April, 2001, with an idea or two about how to tackle the company's problems. First, natch, was to make it operate more efficiently. Johnston is cutting about \$1 billion in costs while spending another billion to upgrade technology—from the supply and distribution system to self-checkout stands. He closed 500 unprofitable stores. And he has introduced a new managerial and financial discipline, including Six Sigma, to the 230,000 employees.

But he also knows that Albertsons—or any retailer, for that matter—can't take on Wal-Mart with greater efficiency and lower prices alone. So Johnston has decided that Albertsons will have to make grocery shopping something it not always is: quick and easy. If all goes as planned, in 18 months shoppers in all 2,500 stores will use handheld scanners that are connected to a company data base and a global-positioning-satellite system. The

devices will read product labels and keep a running tab; they can direct customers to the shortest path to their groceries and alert them to special offers based on past purchases or that a prescription is ready. At the exit, the scanner charges the total to a credit card. No checkout line. No waiting. "The new technology not only allows us to be more efficient, but it also allows us to connect better with customers at the most intimate levels." And this, Johnston hopes, will help Albertsons finally boost sales.

Because it isn't happening any other way. So far, Johnston is squeezing profit out of the grocer but not through sales growth. The 18 percent rise in third-quarter earnings was due mostly to lower costs. Same-store sales growth stayed flat, at 0.3 percent. "Albertsons sales momentum remains very uninspiring," says Goldman Sachs & Co. analyst John Heinbockel. Meanwhile, Wal-Mart could well generate up to \$162 billion annually in "supermarket-type" sales in three years, according to retail consultant Retail Forward Inc. That's more than the combined revenues of the top three national grocers: Kroger, Albertsons, and Safeway.

War with the Workers

Johnston is also dealing with the lingering aftereffects of last year's four-month strike in Southern California, which cost the company \$1.2 billion in lost sales and immeasurable ill will among employees. "You can't differentiate yourself from Wal-Mart through high-quality service at the same time you go to war with your workforce demanding they give up their benefits," says Patrick J. O'Neill, executive vice-president of the United Food & Commercial Workers union.

You might think that Johnston, who likes to talk about motivating employees, would have some regrets about the strike. But it doesn't appear so. "[The strike] was very costly, but [the settlement] was one of the best investments our company ever made," he says. He believes his tough stand allowed him to reach labor agreements elsewhere more readily. That, and direct communication with the employees. When a union in Chicago was sitting on a new contract, Johnston decided to explain the terms in a video he sent to every worker's

home. The contract was approved by the next deadline.

Johnston is continuing the charm offensive with weekly e-mails to all employees, monthly live broadcasts, and regular visits to stores. And he is introducing a seminar on positive thinking. That's not something Joe Albertson might have put much stock in, but then he probably never imagined that Wal-Mart would one day be selling milk and eggs.

Questions

1. Why did Larry Johnston leave his top management position at General Electric to head up the ailing Albertsons grocery chain?
2. What is his vision for Albertsons?
3. How is he seeking to transform Albertsons?
4. How does Johnston motivate and inspire employees?

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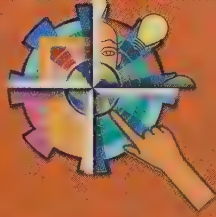
CHAPTER 11

Effective Team Management

Learning Objectives

After studying this chapter, you should be able to:

- Explain why groups and teams are key contributors to organizational effectiveness.
- Identify the different types of groups and teams that help managers and organizations achieve their goals.
- Explain how different elements of group dynamics influence the functioning and effectiveness of groups and teams.
- Explain why it is important for groups and teams to have a balance of conformity and deviance and a moderate level of cohesiveness.
- Describe how managers can motivate group members to achieve organizational goals and reduce social loafing in groups and teams.



Management Snapshot

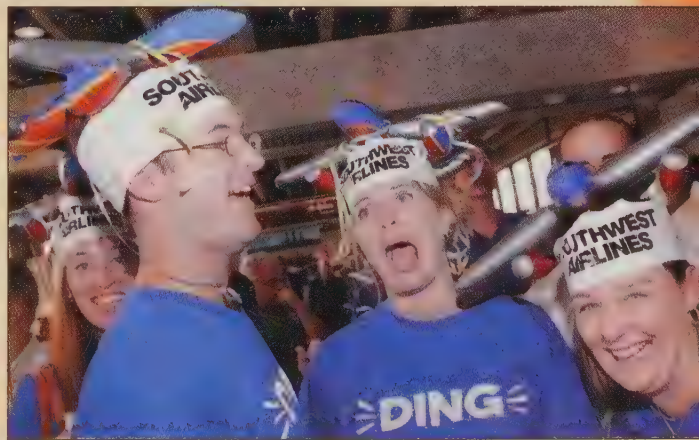
Cohesiveness and Success at Southwest Airlines

How can companies in troubled industries succeed on an ongoing basis?

Southwest Airlines' culture exudes cohesiveness. From hiring people who are fun, friendly, and caring to celebrating and throwing parties on each and every special occasion, Southwest's people-oriented culture emphasizes love, having a good time, excellent customer service, and an esprit de corps second to none.¹ At Southwest's headquarters in Dallas, the walls are covered with photos of employees, their pets, and their families. As Colleen Barrett, Southwest's president and chief operating officer, puts it, "This is an open scrapbook. We aren't uptight. . . . We are having a *party!* . . . We really do everything with passion. We scream at each other and we hug each other."²

Teams at Southwest are known for their cohesiveness and esprit de corps as well. Take the case of the marketing team that Benjean Riedman leads as a Southwest district marketing manager in Seattle.³ Team members work well together, help one another out, and are driven to market and sell

Southwest in the Pacific Northwest. The team also gives to the local communities they serve through charitable activities and volunteer work. Riedman, for example, is on the grant and auction committees for the Ronald McDonald House in Seattle. Team members count on one another, and as Riedman puts it, "They are more than co-workers, they are family."⁴



Southwest Airlines employees Steve Hubbell (left), Rachel Hubbell (center), and Amy Weaver (right) participate in a welcoming ceremony at Philadelphia International Airport May 2004, for the start of service in this new location. Teamwork has been a cornerstone Southwest's success.

Southwest Airlines' continuing success in an industry and environment in which other major airlines are floundering reinforces cohesiveness at the team and organizational

levels.⁵ After the tragic terrorist attacks on September 11, 2001, when other airlines were forced to lay off employees and still lost money, Southwest continued to earn a profit without having to lay off employees.⁶ Southwest's earnings in the first quarter of 2005 were \$76 million, almost triple the 2004 first quarter earnings of \$26 million.⁷ While Southwest's zany culture emphasizes playfulness, keeping costs low and providing excellent customer service are serious business at Southwest. From no assigned seats, meals, or entertainment on flights (except for that provided by witty flight attendants) to flying only Boeing 737s, Southwest's commitment

to low costs is always on the front burner.⁸ As all airlines have found their costs rising, due in part to rising fuel costs, Southwest has found new ways to cut costs. For example, Southwest recently closed three of its reservation centers to cut costs as more and more travelers are purchasing tickets online and is increasing its use of self-service check-in at airports.⁹ Steps such as these will help to ensure Southwest's continued success; and success helps maintain cohesiveness at Southwest. As Southwest's legendary founder and chairman, Herb Kelleher, puts it, "We run this company to prepare ourselves for the bad times, which always come in business."¹⁰

Overview

Southwest Airlines is not alone in using groups and teams to produce goods and services that best meet customers' needs.

Managers in large companies such as Du Pont, Microsoft, and Ford and in small companies such as Web Industries, Perdue Farms, and Risk International Services are all relying on teams to help them gain a competitive advantage.¹¹ In this chapter we look in detail at how groups and teams can contribute to organizational effectiveness and the types of groups and teams used in organizations. We discuss how different elements of group dynamics influence the functioning and effectiveness of groups, and we describe how managers can motivate group members to achieve organizational goals and reduce social loafing in groups and teams. By the end of this chapter, you will appreciate why the effective management of groups and teams is a key ingredient for organizational performance and a source of competitive advantage.

group Two or more people who interact with each other to accomplish certain goals or meet certain needs.

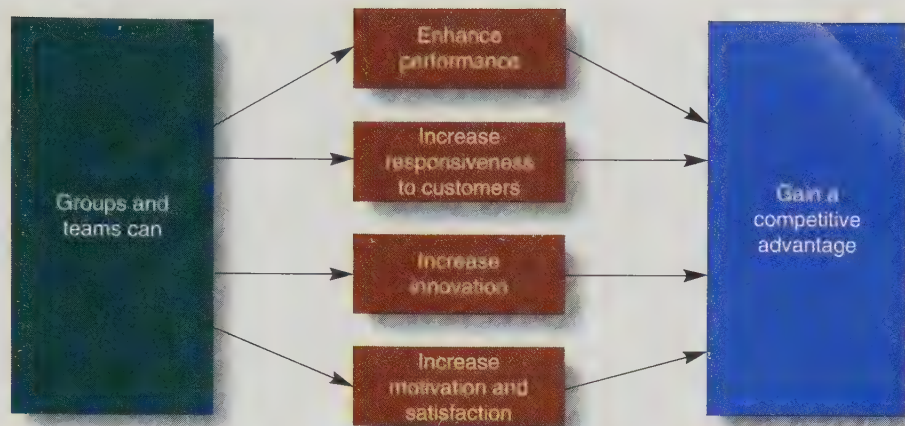
Groups, Teams, and Organizational Effectiveness

A **group** may be defined as two or more people who interact with each other to accomplish certain goals or meet certain needs.¹² A **team** is a group whose members work *intensely* with one another to achieve a specific common goal or objective. As these definitions imply, all teams are groups but not all groups are teams. The two characteristics that distinguish teams from groups are the *intensity* with which team members work together and the presence of a *specific, overriding team goal or objective*.

team A group whose members work intensely with one another to achieve a specific common goal or objective.

As described in the "Management Snapshot," members of teams in Southwest Airlines work together intensely to achieve their goals. In contrast, the accountants who work in a small CPA firm are a group: They may interact with one another to achieve goals such as keeping up to date on the latest changes in accounting rules and regulations, maintaining a smoothly functioning office, satisfying clients, and attracting new clients. But they are not a team because they do not work intensely with one another. Each accountant concentrates on serving the needs of his or her own clients.

Figure 11.1
Groups' and
Teams'
Contributions to
Organizational
Effectiveness



Because all teams are also groups, whenever we use the term *group* in this chapter, we are referring to both groups *and* teams. As you might imagine, because members of teams work intensely together, teams can sometimes be difficult to form and it may take time for members to learn how to effectively work together. Groups and teams can help an organization gain a competitive advantage because they can (1) enhance its performance, (2) increase its responsiveness to customers, (3) increase innovation, and (4) increase employees' motivation and satisfaction (see Figure 11.1). In this section, we look at each of these contributions in turn.

Groups and teams as performance enhancers

synergy Performance gains that result when individuals and departments coordinate their actions.

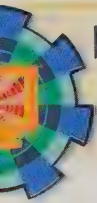
One of the main advantages of using groups is the opportunity to obtain a type of **synergy**: People working in a group are able to produce more or higher-quality outputs than would have been produced if each person had worked separately and all their individual efforts were later combined. The essence of synergy is captured in the saying “The whole is more than the sum of its parts.” Factors that can contribute to synergy in groups include the ability of group members to bounce ideas off one another, to correct one another's mistakes, to solve problems immediately as they arise, to bring a diverse knowledge base to bear on a problem or goal, and to accomplish work that is too vast or all-encompassing for any one individual to achieve on his or her own.

To take advantage of the potential for synergy in groups, managers need to make sure that groups are composed of members who have complementary skills and knowledge relevant to the group's work. For example, at Hallmark Cards, synergies are created by bringing together all the different functions needed to create and produce a greeting card in a cross-functional team (a team composed of members from different departments or functions). For instance, artists, writers, designers, and marketing experts work together as members of a team to develop new cards.¹³

At Hallmark, the skills and expertise of the artists complement the contributions of the writers and vice versa. Managers also need to give groups enough autonomy so that the groups, rather than the manager, are solving problems and determining

how to achieve goals and objectives, as is true in the cross-functional teams at Hallmark. To promote synergy, managers need to empower their subordinates and be coaches, guides, and resources for groups while refraining from playing a more directive or supervisory role. The potential for synergy in groups may be the reason why more and more managers are incorporating empowerment into their personal leadership styles (see Chapter 10).

When tasks are complex and involve highly sophisticated and rapidly changing technologies, achieving synergies in teams often hinges on having the appropriate mix of backgrounds and areas of expertise represented on the team. In large organizations with operations in many states and countries, it is often difficult for managers to determine which employees might have the expertise needed on a particular team or for a certain project. As profiled in the following “Information Technology Byte,” new software applications can help managers identify employees with the expertise needed to achieve real synergies.



Information Technology Byte

Identifying Expertise to Achieve Synergies

Lockheed Martin Corporation has over 130,000 employees working in 939 different locations in over 450 cities in the United States and around the world.¹⁴ These vast human resources provide Lockheed Martin with a tremendous amount of expertise to draw on to solve vexing problems and better meet customers' needs. However, it is a real challenge for managers to identify who in the company might actually have the expertise needed for a particular project or team.

Enter ActiveNet, a software application provided by Tacit Knowledge Systems Inc. ActiveNet scans documents in a company's computer systems, ranging from emails and instant messages to Word and PowerPoint documents, to identify areas of expertise based on what people write and the content of documents they produce;¹⁵ the software creates searchable employee profiles based on this content.¹⁶ For example, a Lockheed team of researchers in California was concerned about the potential for condensation to accumulate in missile canisters. Given all the work Lockheed does with missiles, it was likely that someone in the company had worked on this problem before. Through ActiveNet, the team was able to identify a researcher working in another California facility who had expertise in this area.¹⁷

Northrop Grumman has over 10,000 employees and faces similar challenges in identifying expertise needed to achieve synergies.¹⁸ For example, when Werner Hinz, a Grumman engineer, was preparing a bid for the Pentagon to develop a new, unmanned airplane that could travel faster than the speed of sound, he needed someone with expertise in hypersonics on his team. Hinz couldn't think of any employees he knew with this expertise, so he used ActiveNet by typing in key phrases. ActiveNet provided Hinz with the name of an employee he had actually met and who worked in the same building as Hinz but whom Hinz did not know much about; after speaking to the employee on the phone, Hinz knew he had found the hypersonics expert he needed on his team to prepare the bid. (Hinz's team eventually was awarded a Pentagon contract of \$1.5 million to design the new plane.)¹⁹

While an ActiveNet license is not inexpensive—it costs about \$170 for each employee profile—it can help managers identify expertise needed for synergies in teams by allowing them to search employee profiles. ActiveNet also has privacy protections in place. For example, employees determine who can access which parts of their profiles, and the system does not keep copies of documents after they have been scanned for relevant content. And once ActiveNet identifies an individual in a content domain with regard to a particular query, that individual is contacted first, before his or her name is passed on to the person seeking expertise, to see if he or she wants to make contact with the person making the query, provide information anonymously, or ignore the query. After September 11, 2001, the CIA began using ActiveNet in its counterterrorist efforts.²⁰ To the extent that ActiveNet can help managers like Hinz find employees with needed expertise, it may help them achieve synergies in teams.

Groups, teams, and responsiveness to customers

Being responsive to customers is not always easy. In manufacturing organizations, for example, customers' needs and desires for new and improved products have to be balanced against engineering constraints, production costs and feasibilities, government safety regulations, and marketing challenges. In service organizations such as health maintenance organizations (HMOs), being responsive to patients' needs and desires for prompt, high-quality medical care and treatment has to be balanced against meeting physicians' needs and desires and keeping health care costs under control. Being responsive to customers often requires the wide variety of skills and expertise found in different departments and at different levels in an organization's hierarchy. Sometimes, for example, employees at lower levels in an organization's hierarchy, such as sales representatives for a computer company, are closest to its customers and the most attuned to their needs. However, lower-level employees like salespeople often lack the technical expertise needed to come up with new product ideas; such expertise is found in the research and development department. Bringing salespeople, research and development experts, and members of other departments together in a group or cross-functional team can enhance responsiveness to customers. Consequently, when managers form a team, they need to make sure that the diversity of expertise and knowledge needed to be responsive to customers exists within the team; this is why cross-functional teams are so popular.

In a cross-functional team, the expertise and knowledge in different organizational departments are brought together in the skills and knowledge of the team members. Managers of high-performing organizations are careful to determine which types of expertise and knowledge are required for teams to be responsive to customers, and they use this information in forming teams.

Teams and innovation

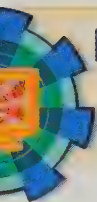
Innovation, the implementation of creative ideas for new products, new technologies, new services, or even new organizational structures, is essential for gaining and maintaining a competitive advantage. Often, an individual working alone does not possess the extensive and diverse set of skills, knowledge, and expertise required

for successful innovation. Managers can better encourage innovation by creating teams of diverse individuals who together have the knowledge relevant to a particular type of innovation rather than by relying on individuals working alone.

Using teams to innovate has other advantages as well. First, team members can often uncover one another's errors or false assumptions; an individual acting alone would not be able to do this. Second, team members can critique one another's approaches when need be and build off one another's strengths while compensating for weaknesses, one of the advantages of devil's advocacy discussed in Chapter 5.

To further promote innovation, managers are well advised to empower teams and make their members fully responsible and accountable for the innovation process. The manager's role is to provide guidance, assistance, coaching, and the resources team members need and *not* to closely direct or supervise their activities. To speed innovation, managers also need to form teams in which each member brings some unique resource to the team, such as engineering prowess, knowledge of production, marketing expertise, or financial savvy. Successful innovation sometimes requires that managers form teams with members from different countries and cultures.

Amazon uses teams to spur innovation, and many of the unique features on its Web site that enable it to be responsive to customers and meet their needs have been developed by teams, as indicated in the following "Information Technology Byte."



Information Technology Byte

Pizza Teams at Amazon

Jeff Bezos, founder and CEO of Amazon, is a firm believer in the power of teams to spur innovation. At Amazon, teams have considerable autonomy to develop their ideas and experiment without interference from managers or other groups. And teams are kept deliberately small. According to Bezos, no team should need more than two pizzas to feed its members. If more than two pizzas are needed to nourish a team, the team is too large. Thus, teams at Amazon typically have no more than about five to seven members.²¹



At Amazon, teams adhere to the two-pizza rule; that is, no team should need more than two pizzas to feed its members.

"Pizza teams" have come up with unique and popular innovations that individuals working alone might never have thought of. A team developed the "Gold Box" icon that customers can click on to receive special offers that expire within an hour of opening the treasure chest. Another team developed "Bottom of the Page Deals"—very low priced offers for everyday goods such as batteries and power bars.²² And "Search Inside the Book," a massive undertaking that allows customers to search and read content from over 100,000 books, had its origins in a team.²³

While Bezos gives teams autonomy to develop and run with their ideas, he also believes in the careful analysis and testing of ideas. A great advocate of the power of facts, data, and analysis, Bezos feels

that whenever an idea can be tested through analysis, analysis should rule the day. When an undertaking is just too large or too uncertain or when data are lacking and hard to come by, Bezos and other experienced top managers make the final call.²⁴ But in order to make such judgment calls about implementing new ideas (either by data analysis or by expert judgment), what really is needed are truly creative ideas. To date, teams have played a very important role in generating ideas that have helped Amazon be responsive to its customers, having a widely known Internet brand name, riding out the dot-com bust, and being the highly successful and innovative company it is today.²⁵

Groups and teams as motivators

Managers often decide to form groups and teams to accomplish organizational goals and then find that using groups and teams brings additional benefits. Members of groups, and especially members of teams (because of the higher intensity of interaction in teams), are likely to be more satisfied than they would have been if they were working on their own. The experience of working alongside other highly charged and motivated people can be very stimulating. In addition, working on a team can be very motivating: Team members more readily see how their efforts and expertise directly contribute to the achievement of team and organizational goals, and they feel personally responsible for the outcomes or results of their work.

The increased motivation and satisfaction that can accompany the use of teams can also lead to other outcomes, such as lower turnover. This has been Frank B. Day's experience as founder and CEO of Rock Bottom Restaurants Inc. To provide high-quality customer service, Day has organized the restaurants' employees into wait staff teams, whose members work together to refill beers, take orders, bring hot chicken enchiladas to the tables, or clear off the tables. Team members share the burden of undesirable activities and unpopular shift times, and customers no longer have to wait until a particular waitress or waiter is available. Motivation and satisfaction levels in Rock Bottom restaurants seem to be higher than in other restaurants, and turnover is about one-half of that experienced in other U.S. restaurant chains.²⁶

Working in a group or team can also satisfy organizational members' needs for engaging in social interaction and feeling connected to other people. For workers who perform highly stressful jobs, such as hospital emergency and operating room staff, group membership can be an important source of social support and motivation. Family members or friends may not be able to fully understand or appreciate some sources of work stress that these group members experience firsthand. Moreover, group members may cope better with work stressors when they are able to share them with other members of their group. In addition, groups often devise techniques to relieve stress, such as the telling of jokes among hospital operating room staff.

Why do managers in all kinds of organizations rely so heavily on groups and teams? Effectively managed groups and teams can help managers in their quest for high performance, responsiveness to customers, and employee motivation. Before explaining how managers can effectively manage groups, however, we will describe the types of groups that are formed in organizations.

Types of Groups and Teams

formal group A group that managers establish to achieve organizational goals.

informal group A group that managers or nonmanagerial employees form to help achieve their own goals or meet their own needs.

To achieve their goals of high performance, responsiveness to customers, innovation, and employee motivation, managers can form various types of groups and teams (see Figure 11.2). **Formal groups** are those managers establish

to achieve organizational goals. The formal work groups are *cross-functional* teams composed of members from different departments, such as those at Hallmark Cards, and *cross-cultural* teams composed of members from different cultures or countries, such as the teams at global carmakers. As you will see, some of the groups discussed in this section also can be considered to be cross-functional (if they are composed of members from different departments) or cross-cultural (if they are composed of members from different countries or cultures).

Sometimes organizational members, managers or nonmanagers, form groups because they feel that groups will help them achieve their own goals or meet their own needs (for example, the need for social interaction). Groups formed in this way are **informal groups**. Four nurses who work in a hospital and have lunch together twice a week constitute an informal group.

The top-management team

top-management team A group composed of the CEO, the president, and the heads of the most important departments.

A central concern of the CEO and president of a company is to form a **top-management team** to help the organization achieve its mission and goals. Top-management teams are responsible for developing the strategies that result in an organization's competitive advantage; most have between five and seven members. In forming their top-management teams, CEOs are well advised to stress diversity—diversity in expertise, skills, knowledge, and experience. Thus, many top-management teams are also cross-functional teams: They are composed of members from different departments, such as finance, marketing, production, and engineering. Diversity helps ensure that the top-management team will have all the background and resources it needs to make good decisions. Diversity also helps guard against *groupthink*, faulty group decision making that results when group members strive for agreement at the expense of an accurate assessment of the situation (see Chapter 5).

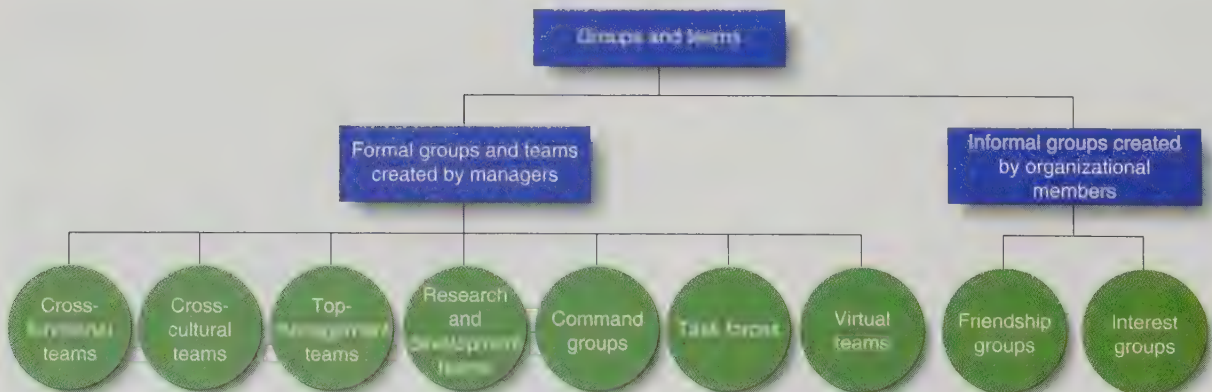


Figure 11.2

Types of Groups and Teams in Organizations

Research and development teams

research and development team

A team whose members have the expertise and experience needed to develop new products.

Managers in pharmaceuticals, computers, electronics, electronic imaging, and other high-tech industries often create **research and development teams** to develop new products. Eric Fossum, for example, a researcher and manager with NASA's Jet Propulsion Laboratory at the California Institute of Technology, formed and heads a three-member R&D team that is developing a camera so small that its basic operational parts can fit on a single computer chip.²⁷ Managers select R&D team members on the basis of their expertise and experience in a certain area. Sometimes R&D teams are cross-functional teams with members from departments such as engineering, marketing, and production in addition to members from the research and development department.

Command groups

command group

A group composed of subordinates who report to the same supervisor; also called *department* or *unit*.

Subordinates who report to the same supervisor compose a **command group**. When top managers design an organization's structure and establish reporting relationships and a chain of command, they are essentially creating command groups. Command groups, often called *departments* or *units*, perform a significant amount of the work in many organizations. In order to have command groups that help an organization gain a competitive advantage, managers not only need to motivate group members to perform at a high level but also need to be effective leaders.

Task forces

task force A committee of managers or nonmanagerial employees from various departments or divisions who meet to solve a specific, mutual problem; also called *ad hoc committee*.

Managers form **task forces** to accomplish specific goals or solve problems in a certain time period; task forces are sometimes called *ad hoc committees*. For example, Michael Rider, owner and top manager of a chain of six gyms and fitness centers in the Midwest, created a task force composed of the general managers of each of the six gyms to determine whether the fitness centers should institute a separate fee schedule for customers who wanted to use the centers only for aerobics classes (and not use other facilities such as weights, steps, tracks, and swimming pools). The task force was given three months to prepare a report summarizing the pros and cons of the proposed change in fee schedules. Once the task force completed its report and reached the conclusion that the change in fee structure probably would reduce revenues rather than increase them and thus should not be implemented, it was disbanded. As in Rider's case, task forces can be a valuable tool for busy managers who do not have the time to personally explore an important issue in depth.

Self-managed work teams

self-managed work team A group of employees who supervise their own activities and monitor the quality of the goods and services they provide.

Self-managed work teams are teams in which team members are empowered and have the responsibility and autonomy to complete identifiable pieces of work. On a day-to-day basis, team members decide what the team will do, how it will do it, and which team members will perform which specific tasks.²⁸ Managers provide self-managed work teams with their overall goals (such as assembling defect-free computer keyboards) but let team members decide how to meet those goals. Managers usually form self-managed work teams to improve quality, increase motivation and satisfaction, and lower costs. Often, by creating self-managed work teams, they combine tasks that individuals working separately used to perform, so the

team is responsible for the whole set of tasks that yields an identifiable output or end product.

In response to increasing competition, Johnson Wax, maker of well-known household products including Pledge furniture polish, Glade air freshener, and Windex window cleaner, formed self-managed work teams to find ways to cut costs. Traditionally, Johnson Wax used assembly-line production, in which workers were not encouraged or required to do much real thinking on the job, let alone determine how to cut costs. Things could not be more different at Johnson Wax now. Consider, for example, the nine-member self-managed work team that is responsible for molding plastic containers. Team members choose their own leader, train new members, have their own budget to manage, and are responsible for figuring out how to cut costs of molding plastic containers. Kim Litrenta, a 17-year veteran of Johnson's Waxdale, Wisconsin, plant sums up the effects of the change from assembly-line production to self-managed work teams this way: "In the past you'd have no idea how much things cost because you weren't involved in decisions. Now it's amazing how many different ways people try to save money."²⁹

Managers can take a number of steps to ensure that self-managed work teams are effective and help an organization gain a competitive advantage:³⁰

- Give teams enough responsibility and autonomy to be truly self-managing. Refrain from telling team members what to do or solving problems for them even if you (as a manager) know what should be done.
- Make sure that a team's work is sufficiently complex so that it entails a number of different steps or procedures that must be performed and results in some kind of finished end product.
- Carefully select members of self-managed work teams. Team members should have the diversity of skills needed to complete the team's work, have the ability to work with others, and want to be part of a team.
- As a manager, realize that your role vis-à-vis self-managed work teams calls for guidance, coaching, and supporting, not supervising. You are a resource for teams to turn to when needed.
- Analyze what type of training team members need and provide it. Working in a self-managed work team often requires that employees have more extensive technical and interpersonal skills.

Managers in a wide variety of organizations have found that self-managed work teams help the organization achieve its goals.³¹ However, self-managed work teams can run into trouble. Members are often reluctant to discipline one another by withholding bonuses from members who are not performing up to par or by firing members.³² Buster Jarrell, a manager who oversees self-managed work teams in AES Corporation's Houston plant, has found that although self-managed work teams are highly effective, they have a very difficult time firing team members who are performing poorly.³³

Virtual teams

Virtual teams are teams whose members rarely or never meet face-to-face but, rather, interact by using various forms of information technology such as email, computer networks, telephone, fax, and videoconferences. As organizations

virtual team A team whose members rarely or never meet face-to-face but, rather, interact by using various forms of information technology such as email, computer networks, telephone, fax, and videoconferences.

become increasingly global, with operations in far-flung regions of the world, and as the need for specialized knowledge increases due to advances in technology, managers can create virtual teams to solve problems or explore opportunities without being limited by the fact that team members need to be working in the same geographic location.³⁴

Take the case of an organization that has manufacturing facilities in Australia, Canada, the United States, and Mexico and is encountering a quality problem in a complex manufacturing process. Each of its manufacturing facilities has a quality control team headed by a quality control manager. The vice president for production does not try to solve the problem by forming and leading a team at one of the four manufacturing facilities; instead, she forms and leads a virtual team composed of the quality control managers of the four plants and the plants' general managers. When these team members communicate via email and videoconferencing, a wide array of knowledge and experience is brought to bear to solve the problem.

The principal advantage of virtual teams is that they enable managers to disregard geographic distances and form teams whose members have the knowledge, expertise, and experience to tackle a particular problem or take advantage of a specific opportunity.³⁵ Virtual teams also can include members who are not actually employees of the organization itself; a virtual team might include members of a company that is used for outsourcing. More and more companies, including Compaq-Hewlett-Packard, Price-WaterhouseCoopers, Lotus Development, Kodak, Whirlpool, and VeriFone, are either using or exploring the use of virtual teams.³⁶

There are two forms of information technologies that members of virtual teams rely on, synchronous technologies and asynchronous technologies.³⁷ *Synchronous technologies* enable virtual team members to communicate and interact with one another in real time simultaneously and include videoconferencing, teleconferencing, and electronic meetings. *Asynchronous technologies* delay communication and include email, electronic bulletin boards, and Internet Web sites. Many virtual teams use both kinds of technology, depending on what projects they are working on.

Increasing globalization is likely to result in more organizations relying on virtual teams to a greater extent.³⁸ One of the major challenges members of virtual teams face is building a sense of camaraderie and trust among team members who rarely, if ever, meet face-to-face. To address this challenge, some organizations schedule recreational activities, such as ski trips, so that virtual team members can get together. Other organizations make sure that virtual team members have a chance to meet in person soon after the team is formed and then schedule periodic face-to-face meetings to promote trust, understanding, and cooperation in the teams.³⁹ The need for such meetings is underscored by research that suggests that while some virtual teams can be as effective as teams that meet face-to-face, virtual team members might be less satisfied with teamwork efforts and have fewer feelings of camaraderie or cohesion. (Group cohesiveness is discussed in more detail later in the chapter.)⁴⁰

Research also suggests that it is important for managers to keep track of virtual teams and intervene when necessary by, for example, encouraging members of teams who do not communicate often enough to monitor their team's progress and make sure that team members actually have the time, and are recognized for, their virtual teamwork.⁴¹ Additionally, when virtual teams are experiencing downtime or rough spots, managers might try to schedule face-to-face team time to bring team members together and help them focus on their goals.⁴²

Friendship groups like the one pictured here can be beneficial to an organization. They help satisfy employees' needs for interpersonal interaction, provide social support in times of stress, and can increase job satisfaction. Since group members often discuss work-related problems, they may even end up generating solutions that can be used on the job.



Friendship groups

friendship group

An informal group composed of employees who enjoy one another's company and socialize with one another.

The groups described so far are formal groups created by managers. **Friendship groups** are informal groups composed of employees who enjoy one another's company and socialize with one another. Members of friendship groups may have lunch together, take breaks together, or meet after work for meals, sports, or other activities. Friendship groups help satisfy employees' needs for interpersonal interaction, can provide needed social support in times of stress, and can contribute to people's feeling good at work and being satisfied with their jobs. Managers themselves often form friendship groups. The informal relationships that managers build in friendship groups can often help them solve work-related problems because members of these groups typically discuss work-related matters and offer advice.

Interest groups

interest group

An informal group composed of employees seeking to achieve a common goal related to their membership in an organization.

Employees form informal **interest groups** when they seek to achieve a common goal related to their membership in an organization. Employees may form interest groups, for example, to encourage managers to consider instituting flexible working hours, providing on-site child care, improving working conditions, or more proactively supporting environmental protection. Interest groups can provide managers with valuable insights into the issues and concerns that are foremost in employees' minds. They also can signal the need for change.

Group Dynamics

The ways in which groups function and, ultimately, their effectiveness hinge on group characteristics and processes known collectively as *group dynamics*. In this section, we discuss five key elements of group dynamics: group size and roles; group leadership; group development; group norms; and group cohesiveness.

Group size and roles

Managers need to take group size and group roles into account as they create and maintain high-performing groups and teams.

GROUP SIZE The number of members in a group can be an important determinant of members' motivation and commitment and group performance. There are several advantages to keeping a group relatively small—between two and nine members. Compared with members of large groups, members of small groups tend to (1) interact more with each other and find it easier to coordinate their efforts, (2) be more motivated, satisfied, and committed, (3) find it easier to share information, and (4) be better able to see the importance of their personal contributions for group success. A disadvantage of small rather than large groups is that members of small groups have fewer resources available to accomplish their goals.

Large groups—with 10 or more members—also offer some advantages. They have more resources at their disposal to achieve group goals than small groups do. These resources include the knowledge, experience, skills, and abilities of group members as well as their actual time and effort. Large groups also enable managers to obtain the advantages stemming from the **division of labor**—splitting the work to be performed into particular tasks and assigning tasks to individual workers. Workers who specialize in particular tasks are likely to become skilled at performing those tasks and contribute significantly to high group performance.

The disadvantages of large groups include the problems of communication and coordination and the lower levels of motivation, satisfaction, and commitment that members of large groups sometimes experience. It is clearly more difficult to share information with, and coordinate the activities of, 16 people rather than 8 people. Moreover, members of large groups might not think that their efforts are really needed and sometimes might not even feel a part of the group.

In deciding on the appropriate size for any group, managers attempt to gain the advantages of small-group size and, at the same time, form groups with sufficient resources to accomplish their goals and have a well-developed division of labor. As a general rule of thumb, groups should have no more members than necessary to achieve a division of labor and provide the resources needed to achieve group goals. In R&D teams, for example, group size is too large when (1) members spend more time communicating what they know to others than applying what they know to solve problems and create new products, (2) individual productivity decreases, and (3) group performance suffers.⁴³

GROUP ROLES A **group role** is a set of behaviors and tasks that a member of a group is expected to perform because of his or her position in the group. Members of cross-functional teams, for example, are expected to perform roles relevant to their special areas of expertise. In our earlier example of cross-functional teams at Hallmark Cards, it is the role of writers on the teams to create verses for new cards, the role of artists to draw illustrations, and the role of designers to put verse and artwork together in an attractive and appealing card design. The roles of members of top-management teams are shaped primarily by their areas of expertise—production, marketing, finance, research and development—but members of top-management teams also typically draw on their broad-based expertise as planners and strategists.

In forming groups and teams, managers need to clearly communicate to group members the expectations for their roles in the group, what is required of them, and

division of labor

Splitting the work to be performed into particular tasks and assigning tasks to individual workers.

group role A set of behaviors and tasks that a member of a group is expected to perform because of his or her position in the group.

role making Taking the initiative to modify an assigned role by assuming additional responsibilities.

how the different roles in the group fit together to accomplish group goals. Managers also need to realize that group roles often change and evolve as a group's tasks and goals change and as group members gain experience and knowledge. Thus, to get the performance gains that come from experience or "learning by doing," managers should encourage group members to take the initiative to assume additional responsibilities as they see fit and modify their assigned roles. This process, called **role making**, can enhance individual and group performance.

In self-managed work teams and some other groups, group members themselves are responsible for creating and assigning roles. Many self-managed work teams also pick their own team leaders. When group members create their own roles, managers should be available to group members in an advisory capacity, helping them effectively settle conflicts and disagreements. At Johnsonville Foods, for example, the position titles of first-line managers have been changed to "advisory coach" to reflect the managers' new role vis-à-vis the self-managed work teams they oversee.⁴⁴

Group leadership

All groups and teams need leadership. Indeed, as we discussed in detail in Chapter 10, effective leadership is a key ingredient for high-performing groups, teams, and organizations. Sometimes managers assume the leadership role in groups and teams, as is the case in many command groups and top-management teams. Or a manager may appoint a member of a group who is not a manager to be group leader or chairperson, as is the case in a task force or standing committee. In other cases, group or team members may choose their own leaders, or a leader may emerge naturally as group members work together to achieve group goals. When managers empower members of self-managed work teams, they often let group members choose their own leaders. Some self-managed work teams find it effective to rotate the leadership role among their members. Whether leaders of groups and teams are managers or not, and whether they are appointed by managers or emerge naturally in a group, they play an important role in ensuring that groups and teams perform up to their potential.

Group development over time

As many managers overseeing self-managed teams have learned, it sometimes takes a self-managed work team two or three years to perform up to its true capabilities.⁴⁵ As their experience suggests, what a group is capable of achieving depends in part on its stage of development. Knowing that it takes considerable time for self-managed work teams to get up and running has helped managers have realistic expectations for new teams and know that they need to provide new team members with considerable training and guidance.

Although every group's development over time is somewhat unique, researchers have identified five stages of group development that many groups seem to pass through (see Figure 11.3).⁴⁶ In the first stage, *forming*, members try to get to know one another and reach a common understanding of what the group is trying to accomplish and how group members should behave. During this stage, managers should strive to make each member feel that he or she is a valued part of the group.

In the second stage, *storming*, group members experience conflict and disagreements because some members do not wish to submit to the demands of other group members. Disputes may arise over who should lead the group. Self-managed work

Figure 11.3
Five Stages
of Group
Development



teams can be particularly vulnerable during the storming stage. Managers need to keep an eye on groups at this stage to make sure that conflict does not get out of hand.

During the third stage, *norming*, close ties between group members develop, and feelings of friendship and camaraderie emerge. Group members arrive at a consensus about what goals they should be seeking to achieve and how group members should behave toward one another.

In the fourth stage, *performing*, the real work of the group gets accomplished. Depending on the type of group in question, managers need to take different steps at this stage to help ensure that groups are effective. Managers of command groups need to make sure that group members are motivated and that they are effectively leading group members. Managers overseeing self-managed work teams have to empower team members and make sure that teams are given enough responsibility and autonomy at the performing stage.

The last stage, *adjourning*, applies only to groups that eventually are disbanded, such as task forces. During adjourning a group is dispersed. Sometimes, adjourning takes place when a group completes a finished product, such as when a task force evaluating the pros and cons of providing on-site child care produces a report supporting its recommendation.

Managers should have a flexible approach to group development and should keep attuned to the different needs and requirements of groups at the various stages.⁴⁷ Above all else, and regardless of the stage of development, managers need to think of themselves as *resources* for groups. Thus, managers always should be striving to find ways to help groups and teams function more effectively.

Group norms

All groups, whether top-management teams, self-managed work teams, or command groups, need to control their members' behaviors to ensure that the group performs highly and meets its goals. Assigning roles to each group member is one way to control behavior in groups. Another important way in which groups influence members' behavior is through the development and enforcement of group norms.⁴⁸

Group norms are shared guidelines or rules for behavior that most group members follow. Groups develop norms concerning a wide variety of behaviors, including working hours, the sharing of information among group members, how certain group tasks should be performed, and even how members of a group should dress.

Managers should encourage members of a group to develop norms that contribute to group performance and the attainment of group goals. For example, group norms that dictate that each member of a cross-functional team should always be available for the rest of the team when his or her input is needed, return phone calls as soon as possible, inform other team members of travel plans, and give team members a phone number at which he or she can be reached when traveling on business help to ensure that the team is efficient, performs highly, and achieves its goals. A norm in a command group of secretaries that dictates that secretaries who happen to have a light workload in any given week should help out secretaries with heavier

group norms

Shared guidelines or rules for behavior that most group members follow.



A group of employees volunteering at a food bank packs boxes of food for delivery. While these employees are likely participating at least in part out of a desire to help others, they may also be influenced by group norms encouraging them to conform to group behaviors in order to maintain good relations with co-workers.

workloads helps to ensure that the group completes all assignments in a timely and efficient manner. And a norm in a top-management team that dictates that team members should always consult with one another before making major decisions helps to ensure that good decisions are made with a minimum of errors.

CONFORMITY AND DEVIANCE Group members conform to norms for three reasons: (1) They want to obtain rewards and avoid punishments. (2) They want to imitate group members whom they like and admire. (3) They have internalized the norm and believe it is the right and proper way to behave.⁴⁹ Consider the case of Robert King, who conformed to his department's norm of attending a fund-raiser for a community food bank. King's conformity could be due to (1) his desire to be a member of the group in good standing and to have friendly relationships with other group members

(rewards), (2) his copying the behavior of other members of the department whom he respects and who always attend the fund-raiser (imitating other group members), or (3) his belief in the merits of supporting the activities of the food bank (believing that is the right and proper way to behave).

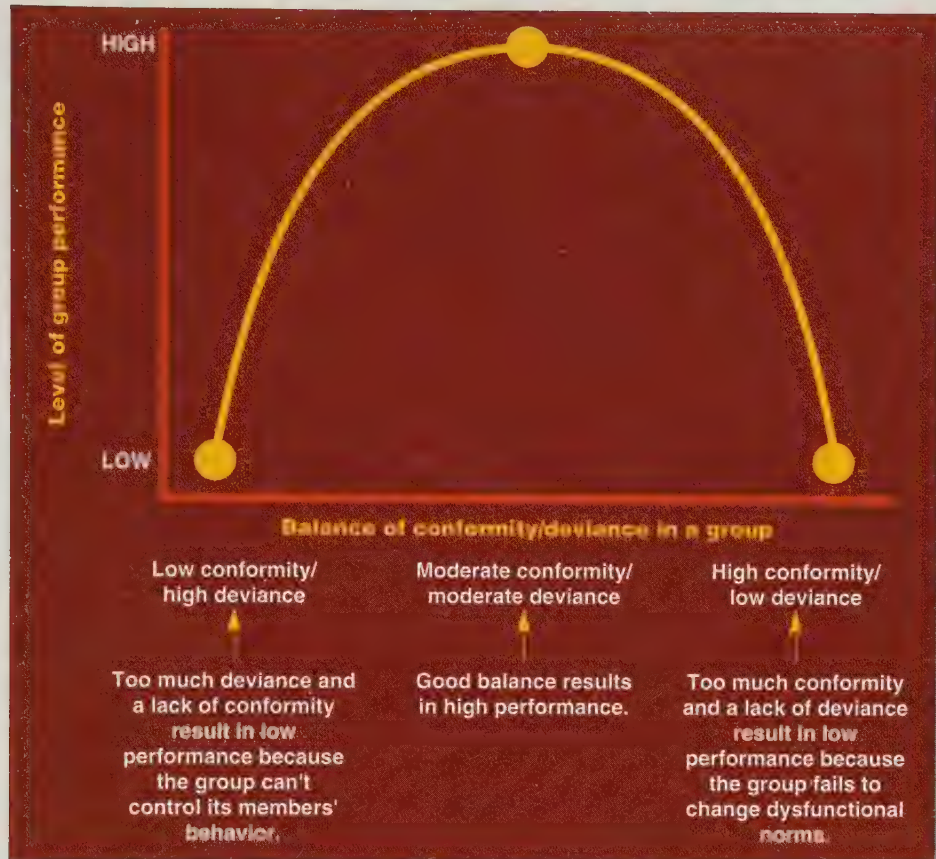
Failure to conform, or deviance, occurs when a member of a group violates a group norm. Deviance signals that a group is not controlling one of its member's behaviors. Groups generally respond to members who behave defiantly in one of three ways:⁵⁰

1. The group might try to get the member to change his or her deviant ways and conform to the norm. Group members might try to convince the member of the need to conform, or they might ignore or even punish the deviant. For example, in a Jacksonville Foods plant Liz Senkbiel, a member of a self-managed work team responsible for weighing sausages, failed to conform to a group norm dictating that group members should periodically clean up an untidy room used to interview prospective employees. Because Senkbiel refused to take part in the team's cleanup efforts, team members reduced her monthly bonus by about \$225 for a two-month period.⁵¹ Senkbiel clearly learned the costs of deviant behavior in her team.
2. The group might expel the member.
3. The group might change the norm to be consistent with the member's behavior.

That last alternative suggests that some deviant behavior can be functional for groups. Deviance is functional for a group when it causes group members to evaluate norms that may be dysfunctional but are taken for granted by the group. Often, group members do not think about why they behave in a certain way or why they follow certain norms. Deviance can cause group members to reflect on their norms and change them when appropriate.

Take the case of a group of receptionists in a beauty salon who followed the norm that all appointments would be handwritten in an appointment book and at the end of each day the receptionist on duty would enter the appointments into the salon's computer system, which printed out the hairdressers' daily schedules. One day, a receptionist decided to enter appointments directly into the computer system

Figure 11.4
Balancing
Conformity
and Deviance
in Groups



at the time they were being made, bypassing the appointment book. This deviant behavior caused the other receptionists to think about why they were using the appointment book in the first place, since all appointments could be entered into the computer directly. After consulting with the owner of the salon, the group changed its norm. Now appointments are entered directly into the computer, which saves time and cuts down on scheduling errors.

ENCOURAGING A BALANCE OF CONFORMITY AND DEVIANCE To effectively help an organization gain a competitive advantage, groups and teams need to have the right balance of conformity and deviance (see Figure 11.4). A group needs a certain level of conformity to ensure that it can control members' behavior and channel it in the direction of high performance and group goal accomplishment. A group also needs a certain level of deviance to ensure that dysfunctional norms are discarded and replaced with functional ones. Balancing conformity and deviance is a pressing concern for all groups, whether they are top-management teams, R&D teams, command groups, or self-managed work teams.

The extent of conformity and reactions to deviance within groups are determined by group members themselves. The three bases for conformity described above are powerful forces that more often than not result in group members' conforming to norms. Sometimes these forces are so strong that deviance rarely occurs in groups, and when it does, it is stamped out.

Managers can take several steps to ensure that there is enough tolerance of deviance in groups so that group members are willing to deviate from dysfunctional norms and, when deviance occurs in their group, reflect on the appropriateness of the violated norm and change the norm if necessary. First, managers can be role models for the groups and teams they oversee. When managers encourage and accept employees' suggestions for changes in procedures, do not rigidly insist that tasks be accomplished in a certain way, and admit when a norm that they once supported is no longer functional, they signal to group members that conformity should not come at the expense of needed changes and improvements. Second, managers should let employees know that there are always ways to improve group processes and performance levels and thus opportunities to replace existing norms with norms that will better enable a group to achieve its goals and perform at a high level. Third, managers should encourage members of groups and teams to periodically assess the appropriateness of their existing norms.

Managers in the innovative design firm Ideo, based in Palo Alto, California have excelled at ensuring that design teams have the right mix of conformity and deviance, resulting in Ideo's designing products in fields ranging from medicine to space travel to computing and personal hygiene, as indicated in the following "Focus on Diversity."



Focus on Diversity

Diversity of Thought and Respect for Ideas Reign at Ideo

Ideo designed many products we now take for granted. Ideo designed the first Apple mouse, the Palm handheld organizer, stand-up toothpaste containers, flexible shelving for offices, self-sealing drink bottles for sports, blood analyzers, and even equipment used in space travel.⁵² Managers and designers at Ideo pride themselves on being experts at the process of innovation in general, rather than in any particular domain. Of course, the company has technical design experts, such as mechanical and electrical engineers, who work on products requiring specialized knowledge, but on the same teams with the engineers might be an anthropologist, a biologist, and a social scientist.⁵³

Essentially, a guiding principle at Ideo is that innovation comes in many shapes and sizes and it is only through diversity in thought that people can recognize opportunities for innovation. To promote such diversity in thought, new product development at Ideo is a team effort.⁵⁴ Moreover, both conformity and deviance are encouraged on Ideo teams.

Deviance, thinking differently, and not conforming to expected ways of doing things and mind-sets are encouraged at Ideo. In fact, innovative ideas often flow when designers try to see things as they really are and are not blinded by thoughts of what is appropriate, what is possible, or how things should be. Often, constraints on new product design are created by designers themselves conforming to a certain mind-set about the nature of a product or what a product can or should do and look like. Ideo designers are encouraged to actively break down these constraints in their design teams.⁵⁵

Managers at Ideo realize the need for a certain amount of conformity so that members of design teams can work effectively together and achieve their goals. Thus, conformity to a few very central norms is emphasized in Ideo teams. These norms include understanding what the team is working on (e.g., the product, market, or client need), observing real people in their natural environments,

visualizing how new products might work and be used, evaluating and refining product prototypes, encouraging wild ideas, and never rejecting an idea simply because it sounds too crazy.⁵⁶ As long as these norms are followed, diversity of thought and even deviance serve to promote innovation at Ideo. In fact, another norm at Ideo is to study “rule breakers”—people who don’t follow instructions for products, for example, or who try to put products to different uses—as these individuals might help designers identify problems with existing products and unmet consumer needs.⁵⁷ All in all, Ideo’s focus on encouraging both deviance and conformity in design teams has benefited all of us as we use Ideo-designed products that seem so familiar, we take them for granted. We forget these products weren’t in existence until a design team at Ideo was called on by a client to develop a new product or improve an existing one.⁵⁸

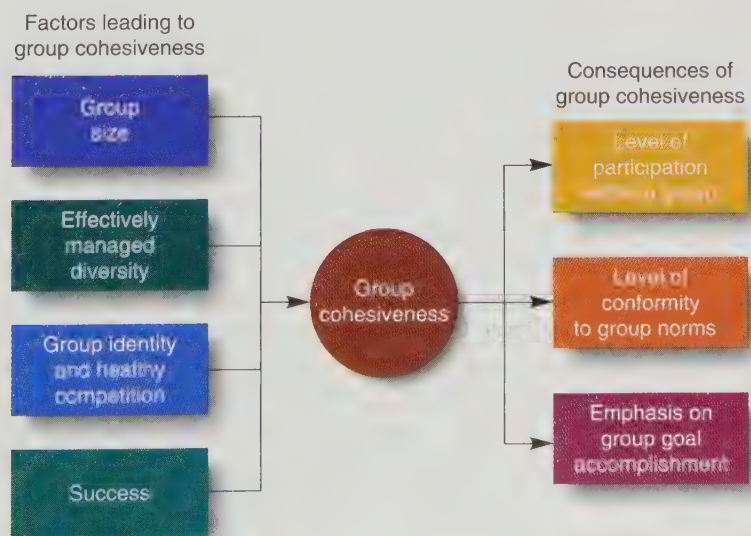
Group cohesiveness

group cohesiveness The degree to which members are attracted to or loyal to their group.

Another important element of group dynamics that affects group performance and effectiveness is **group cohesiveness**, the degree to which members are attracted to or loyal to their group or team.⁵⁹ When group cohesiveness is high, individuals strongly value their group membership, find the group very appealing, and have strong desires to remain a part of the group, as is true in teams at Southwest Airlines in the “Management Snapshot.” When group cohesiveness is low, group members do not find their group particularly appealing and have little desire to retain their group membership. Research suggests that managers should strive to have a moderate level of cohesiveness in the groups and teams they manage because that is most likely to contribute to an organization’s competitive advantage.

CONSEQUENCES OF GROUP COHESIVENESS There are three major consequences of group cohesiveness: level of participation within a group, level of conformity to group norms, and emphasis on group goal accomplishment (see Figure 11.5).⁶⁰

Figure 11.5
Sources and Consequences of Group Cohesiveness



LEVEL OF PARTICIPATION WITHIN A GROUP As group cohesiveness increases, the extent of group members' participation within the group increases. Participation contributes to group effectiveness because group members are actively involved in the group, ensure that group tasks get accomplished, readily share information with each other, and have frequent and open communication (the important topic of communication is covered in depth in Chapter 13).

A moderate level of group cohesiveness helps to ensure that group members actively participate in the group and communicate effectively with one another. The reason why managers may not want to encourage high levels of cohesiveness is illustrated by the example of two cross-functional teams responsible for developing new toys. Members of the highly cohesive Team Alpha often have lengthy meetings that usually start with non-work-related conversations and jokes, meet more often than most of the other cross-functional teams in the company, and spend a good portion of their time communicating the ins and outs of their department's contribution to toy development to other team members. Members of the moderately cohesive Team Beta generally have efficient meetings in which ideas are communicated and discussed as needed, do not meet more often than necessary, and share the ins and outs of their expertise with one another to the extent needed for the development process. Teams Alpha and Beta have both developed some top-selling toys. However, it generally takes Team Alpha 30 percent longer to do so than Team Beta. This is why too much cohesiveness can be too much of a good thing.

LEVEL OF CONFORMITY TO GROUP NORMS Increasing levels of group cohesiveness result in increasing levels of conformity to group norms, and when cohesiveness becomes high, there may be so little deviance in groups that group members conform to norms even when they are dysfunctional. In contrast, low cohesiveness can result in too much deviance and undermine the ability of a group to control its members' behaviors to get things done.

Teams Alpha and Beta in the toy company both had the same norm for toy development. It dictated that members of each team would discuss potential ideas for new toys, decide on a line of toys to pursue, and then have the team member from R&D design a prototype. Recently, a new animated movie featuring a family of rabbits produced by a small film company was an unexpected hit, and major toy companies were scrambling to reach licensing agreements to produce toy lines featuring the rabbits. The top-management team in the toy company assigned Teams Alpha and Beta to develop the new toy lines and to do so quickly to beat the competition.

Members of Team Alpha followed their usual toy development norm even though the marketing expert on the team believed that the process could have been streamlined to save time. The marketing expert on Team Beta urged the team to deviate from its toy development norm. She suggested that the team not have R&D develop prototypes but, instead, modify top-selling toys the company already made to feature rabbits and then reach a licensing agreement with the film company based on the high sales potential (given the company's prior success). Once the licensing agreement was signed, the company could take the time needed to develop innovative and unique rabbit toys with more input from R&D.

As a result of the willingness of the marketing expert on Team Beta to deviate from the norm for toy development, the toy company obtained an exclusive licensing agreement with the film company and had its first rabbit toys on the shelves of stores in a record three months. Groups need a balance of conformity

and deviance, so a moderate level of cohesiveness often yields the best outcome, as it did in the case of Team Beta.

EMPHASIS ON GROUP GOAL ACCOMPLISHMENT As group cohesiveness increases, the emphasis placed on group goal accomplishment also increases within a group. A very strong emphasis on group goal accomplishment, however, does not always lead to organizational effectiveness. For an organization to be effective and gain a competitive advantage, the different groups and teams in the organization must cooperate with one another and be motivated to achieve *organizational goals*, even if doing so sometimes comes at the expense of the achievement of group goals. A moderate level of cohesiveness motivates group members to accomplish both group and organizational goals. High levels of cohesiveness can cause group members to be so focused on group goal accomplishment that they may strive to achieve group goals no matter what—even when doing so jeopardizes organizational performance.

At the toy company, the major goal of the cross-functional teams was to develop new toy lines that were truly innovative, utilized the latest in technology, and were in some way fundamentally distinct from other toys on the market. When it came to the rabbit project, Team Alpha's high level of cohesiveness contributed to its continued emphasis on its group goal of developing an innovative line of toys; thus, the team stuck with its usual design process. Team Beta, in contrast, realized that developing the new line of toys quickly was an important organizational goal that should take precedence over the group's goal of developing pathbreaking new toys, at least in the short run. Team Beta's moderate level of cohesiveness contributed to team members' doing what was best for the toy company in this case.

FACTORS LEADING TO GROUP COHESIVENESS Four factors contribute to the level of group cohesiveness (see Figure 11.5).⁶¹ By influencing these *determinants of group cohesiveness*, managers can raise or lower the level of cohesiveness to promote moderate levels of cohesiveness in groups and teams.

GROUP SIZE As we mentioned earlier, members of small groups tend to be more motivated and committed than members of large groups. Thus, to promote cohesiveness in groups, when feasible, managers should form groups that are small to medium in size (about 2 to 15 members). If a group is low in cohesiveness and large in size, managers might want to consider the feasibility of dividing the group in two and assigning different tasks and goals to the two newly formed groups.

EFFECTIVELY MANAGED DIVERSITY In general, people tend to like and get along with others who are similar to themselves. It is easier to communicate with someone, for example, who shares your values, has a similar background, and has had similar experiences. However, as discussed in Chapter 3, diversity in groups, teams, and organizations can help an organization gain a competitive advantage. Diverse groups often come up with more innovative and creative ideas. One reason why cross-functional teams are so popular in organizations like Hallmark Cards is that the diversity in expertise represented in the teams results in higher levels of team performance.

In forming groups and teams, managers need to make sure that the diversity in knowledge, experience, expertise, and other characteristics necessary for group goal accomplishment is represented in the new groups. Managers then have to make sure that this diversity in group membership is effectively managed so that groups will be cohesive (see Chapter 3).



Employees at the Internet company Google, known as Googlers, play an informal game of street hockey in the company's parking lot two times a week. Friendly competition like this helps build group cohesiveness.

GROUP IDENTITY AND HEALTHY COMPETITION

When group cohesiveness is low, managers can often increase it by encouraging groups to develop their own identities or personalities and to engage in healthy competition. This is precisely what managers at Eaton Corporation, based in Lincoln, Illinois, did. Eaton's employees manufacture products such as engine valves, gears, truck axles, and circuit breakers. Managers at Eaton created self-managed work teams to cut costs and improve performance. They realized, however, that the teams would have to be cohesive to ensure that they would strive to achieve their goals. Managers promoted group identity by having the teams give themselves names such as "The Hoods," "The Worms," and "Scrap Attack" (a team striving to reduce costly scrap-metal waste by 50 percent). Healthy competition among groups is promoted by displaying measures of each team's performance and the extent to which teams have met their goals

on a large TV screen in the cafeteria and by rewarding team members for team performance.⁶²

If groups are too cohesive, managers can try to decrease cohesiveness by promoting organizational (rather than group) identity and making the organization as a whole the focus of the group's efforts. Organizational identity can be promoted by making group members feel that they are valued members of the organization as a whole and by stressing cooperation across groups to promote the achievement of organizational goals. Excessive levels of cohesiveness also can be reduced by reducing or eliminating competition among groups and rewarding cooperation.

SUCCESS When it comes to promoting group cohesiveness, there is more than a grain of truth to the saying "Nothing succeeds like success." As groups become more successful, they become increasingly attractive to their members, and their cohesiveness tends to increase, as is true of teams in Southwest Airlines in the "Management Snapshot." When cohesiveness is low, managers can increase cohesiveness by making sure that a group can achieve some noticeable and visible successes.

Take the case of a group of salespeople in the housewares department of a medium-size department store. The housewares department was recently moved to a corner of the store's basement. Its remote location resulted in low sales because of infrequent customer traffic in that part of the store. The salespeople, who were generally evaluated favorably by their supervisors and were valued members of the store, tried various initiatives to boost sales, but to no avail. As a result of this lack of success and the poor performance of their department, their cohesiveness started to plummet. To increase and preserve the cohesiveness of the group, the store manager implemented a group-based incentive across the store. In any month, members of the group with the best attendance and punctuality records would have their names and pictures posted on a bulletin board in the cafeteria and would each receive a \$50 gift certificate. The housewares group frequently had the best records, and their success on this dimension helped to build and maintain their cohesiveness. Moreover, this initiative boosted attendance and discouraged lateness throughout the store.

Managing Groups and Teams for High Performance

Now that you have a good understanding of why groups and teams are so important for organizations, the types of groups that managers create, and group dynamics, we consider some additional steps that managers can take to make sure groups and teams perform highly and contribute to organizational effectiveness. Managers striving to have top-performing groups and teams need to (1) motivate group members to work toward the achievement of organizational goals, (2) reduce social loafing, and (3) help groups to manage conflict effectively.

Motivating group members to achieve organizational goals

When work is difficult, is tedious, or requires a high level of commitment and energy, managers cannot assume that group members will always be motivated to work toward the achievement of organizational goals. Consider the case of a group of house painters who paint the interiors and exteriors of new homes for a construction company and are paid on an hourly basis. Why should they strive to complete painting jobs quickly and efficiently if doing so will just make them feel more tired at the end of the day and they will not receive any tangible benefits? It makes more sense for the painters to adopt a more relaxed approach, to take frequent breaks, and to work at a leisurely pace. This relaxed approach, however, impairs the construction company's ability to gain a competitive advantage because it raises costs and increases the time needed to complete a new home.

Managers can motivate members of groups and teams to achieve organizational goals and create a competitive advantage by making sure that the members themselves benefit when the group or team performs highly. For example, if members of a self-managed work team know that they will receive a weekly bonus based on team performance, they will be more motivated to perform at a high level.

Managers often rely on some combination of individual and group-based incentives to motivate members of groups and teams to work toward the achievement of organizational goals and a competitive advantage. When individual performance within a group can be assessed, pay is often determined by individual performance or by both individual and group performance. When individual performance within a group cannot be accurately assessed, then group performance should be the key determinant of pay levels. Approximately 75 percent of companies that use self-managed work teams base team members' pay in part on team performance.⁶³ A major challenge for managers is to develop a fair pay system that will lead to both high individual motivation and high group or team performance.

Other benefits that managers can make available to high-performance group members—in addition to monetary rewards—include extra resources such as equipment and computer software, awards and other forms of recognition, and choice of future work assignments. For example, members of self-managed work teams that develop new software at companies like Microsoft often value working on interesting

and important projects; members of teams that have performed highly are rewarded by being assigned to interesting and important new projects.

At Ideo (profiled earlier in “Focus on Diversity”), managers motivate team members by making them feel important. As Tom Kelley, Ideo’s general manager, puts it, “When people feel special, they’ll perform beyond your wildest dreams.”⁶⁴ To make Ideo team members feel special, Ideo managers plan unique and fun year-end parties, give teams the opportunity to take time off if they feel they need or want to, encourage teams to take field trips, and see pranks as a way to incorporate fun into the workplace.⁶⁵

Reducing social loafing in groups

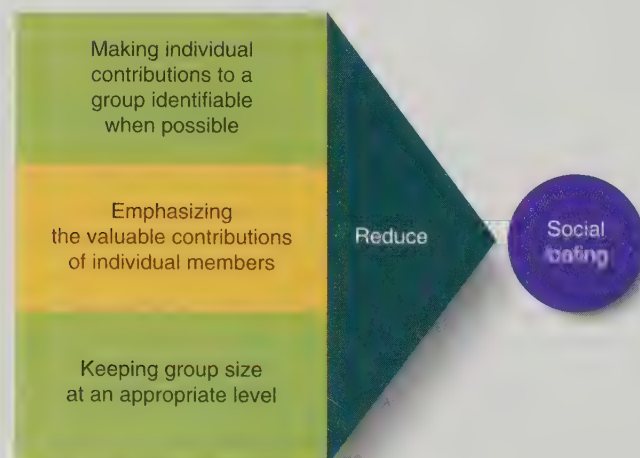
social loafing The tendency of individuals to put forth less effort when they work in groups than when they work alone.

We have been focusing on the steps that managers can take to encourage high levels of performance in groups. Managers, however, need to be aware of an important downside to group and team work: the potential for social loafing, which reduces group performance. **Social loafing** is the tendency of individuals to put forth less effort when they work in groups than when they work alone.⁶⁶ Have you ever worked on a group project in which one or two group members never seemed to be pulling their weight? Have you ever worked in a student club or committee in which some members always seemed to be missing meetings and never volunteered for activities? Have you ever had a job in which one or two of your co-workers seemed to be slacking off because they knew that you or other members of your work group would make up for their low levels of effort? If you have, you have witnessed social loafing in action.

Social loafing can occur in all kinds of groups and teams and in all kinds of organizations. It can result in lower group performance and may even prevent a group from attaining its goals. Fortunately, there are steps managers can take to reduce social loafing and sometimes completely eliminate it; we will look at three (see Figure 11.6).

1. *Make individual contributions to a group identifiable.* Some people may engage in social loafing when they work in groups because they think that they can hide in

Figure 11.6
Three Ways to
Reduce Social
Loafing



the crowd—that no one will notice if they put forth less effort than they should. Other people may think that if they put forth high levels of effort and make substantial contributions to the group, their contributions will not be noticed and they will receive no rewards for their work—so why bother?⁶⁷

One way in which managers can effectively eliminate social loafing is by making individual contributions to a group identifiable so that group members perceive that low and high levels of effort will be noticed and individual contributions evaluated.⁶⁸ Managers can accomplish this by assigning specific tasks to group members and holding them accountable for their completion. Take the case of a group of eight employees responsible for reshelving returned books in a large public library in New York. The head librarian was concerned that there was always a backlog of seven or eight carts of books to be reshelved, even though the employees never seemed to be particularly busy and some even found time to sit down in the current-periodicals section to read newspapers and magazines. The librarian decided to try to eliminate the apparent social loafing by assigning each employee sole responsibility for reshelving a particular section of the library. Because the library's front-desk employees sorted the books by section on the carts as they were returned, holding the shelvees responsible for particular sections was easily accomplished. Once the shelvees knew that the librarian could identify their effort or lack of effort, there were rarely any backlogs of books to be reshelved.

Sometimes the members of a group can cooperate to eliminate social loafing by making individual contributions identifiable. For example, members of a self-managed work team in a small security company who assemble control boxes for home alarm systems start each day by deciding who will perform which tasks that day and how much work each member and the group as a whole should strive to accomplish. Each team member knows that, at the end of the day, the other team members will know exactly how much he or she has accomplished. With this system in place, social loafing never occurs in the team. Remember, however, that in some teams, individual contributions cannot be made identifiable.

2. *Emphasize the valuable contributions of individual members.* Another reason why social loafing may occur is that people sometimes think that their efforts are unnecessary or unimportant when they work in a group. They feel the group will accomplish its goals and perform at an acceptable level whether or not they personally perform at a high level. To counteract this belief, when managers form groups, they should assign individuals to groups on the basis of the valuable contributions that *each* person can make to the group as a whole. Clearly communicating to group members why each person's contributions are valuable to the group is an effective means by which managers and group members themselves can reduce or eliminate social loafing.⁶⁹ This is most clearly illustrated in cross-functional teams where each member's valuable contribution to the team derives from a personal area of expertise. By emphasizing why each member's skills are important, managers can reduce social loafing in such teams.

3. *Keep group size at an appropriate level.* Group size is related to the causes of social loafing we just described. As size increases, identifying individual contributions becomes increasingly difficult and members are increasingly likely to think that their individual contributions are not very important. To overcome this, managers should form groups with no more members than are needed to accomplish group goals and perform highly.⁷⁰

Summary and Review

GROUPS, TEAMS, AND ORGANIZATIONAL EFFECTIVENESS

A group is two or more people who interact with each other to accomplish certain goals or meet certain needs. A team is a group whose members work intensely with one another to achieve a specific common goal or objective. Groups and teams can contribute to organizational effectiveness by enhancing performance, increasing responsiveness to customers, increasing innovation, and being a source of motivation for their members.

TYPES OF GROUPS AND TEAMS Formal groups are groups that managers establish to achieve organizational goals; they include cross-functional teams, cross-cultural teams, top-management teams, research and development teams, command groups, task forces, self-managed work teams, and virtual teams. Informal groups are groups that employees form because they believe that the groups will help them achieve their own goals or meet their needs; they include friendship groups and interest groups.

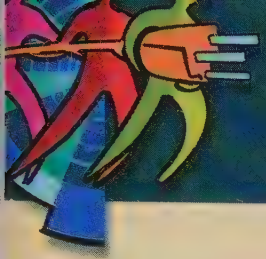
GROUP DYNAMICS Key elements of group dynamics are group size, and roles; group leadership; group development; group norms; and group cohesiveness. The advantages and disadvantages of large and small groups suggest that managers should form groups with no more members than are needed to provide the group with the human resources it needs to achieve its goals and use a division of labor. A group role is a set of behaviors and tasks that a member of a group is expected to perform because of his or her position in the group. All groups and teams need leadership.

Five stages of development that many groups pass through are forming, storming, norming, performing, and adjourning. Group norms are shared rules for behavior that most group members follow. To be effective, groups need a balance of conformity and deviance. Conformity allows a group to control its members' behavior to achieve group goals; deviance provides the impetus for needed change.

Group cohesiveness is the attractiveness of a group or team to its members. As group cohesiveness increases, so, too, does the level of participation and communication within a group, the level of conformity to group norms, and the emphasis on group goal accomplishment. Managers should strive to achieve a moderate level of group cohesiveness in the groups and teams they manage.

MANAGING GROUPS AND TEAMS FOR HIGH PERFORMANCE

To make sure that groups and teams perform highly, managers need to motivate group members to work toward the achievement of organizational goals and reduce social loafing. Managers can motivate members of groups and teams to work toward the achievement of organizational goals by making sure that members personally benefit when the group or team performs well.



Management in Action

Topics for Discussion and Action

Discussion

1. Why do all organizations need to rely on groups and teams to achieve their goals and gain a competitive advantage?
2. What kinds of employees would prefer to work in a virtual team? What kinds of employees would prefer to work in a team that meets face-to-face?
3. Think about a group that you are a member of, and describe that group's current stage of development. Does the development of this group seem to be following the forming, storming, norming, performing, and adjourning stages described in the chapter?
4. Discuss the reasons why too much conformity can hurt groups and their organizations.
5. Why do some groups have very low levels of cohesiveness?
6. Imagine that you are the manager of a hotel. What steps will you take to reduce social loafing by members of

the cleaning staff who are responsible for keeping all common areas and guest rooms spotless?

Action

7. Interview one or more managers in an organization in your local community to identify the types of groups and teams that the organization uses to achieve its goals. What challenges do these groups and teams face?



Building Management Skills

Diagnosing Group Failures

Think about the last dissatisfying or discouraging experience you had as a member of a group or team. Perhaps the group did not accomplish its goals, perhaps group members could agree about nothing, or perhaps there was too much social loafing. Now answer the following questions:

1. What type of group was this?
2. Were group members motivated to achieve group goals? Why or why not?
3. How large was the group, and what group roles did members play?
4. What were the group's norms? How much conformity and deviance existed in the group?
5. How cohesive was the group? Why do you think the group's cohesiveness was at this level? What consequences did this level of group cohesiveness have for the group and its members?
6. Was social loafing a problem in this group? Why or why not?
7. What could the group's leader or manager have done differently to increase group effectiveness?
8. What could group members have done differently to increase group effectiveness?





Small Group Breakout Exercise

Creating a Cross-Functional Team

Form groups of three or four people, and appoint one member as the spokesperson who will communicate your findings to the whole class when called on by the instructor. Then discuss the following scenario.

You are a group of managers in charge of food services for a large state university in the Midwest. Recently a survey of students, faculty, and staff was conducted to evaluate customer satisfaction with the food services provided by the university's eight cafeterias. The results were disappointing, to put it mildly. Complaints ranged from dissatisfaction with the type and range of meals and snacks provided, operating hours,

and food temperature to frustration about unresponsiveness to current concerns about low-carbohydrate diets and the needs of vegetarians. You have decided to form a cross-functional team that will further evaluate reactions to the food services and will develop a proposal for changes to be made to increase customer satisfaction.

1. Indicate who should be on this important cross-functional team and explain why.

- 2.** Describe the goals the team should be striving to achieve.
- 3.** Describe the different roles that will need to be performed in this team.
- 4.** Describe the steps you will take to help ensure that the team has a good balance between conformity and deviance and has a moderate level of cohesiveness.



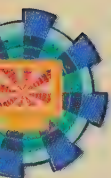
Be the Manager

You were recently hired in a boundary-spanning role for the global unit of an educational and professional publishing company. The company is headquartered in New York (where you work) and has divisions in multiple countries. Each division is responsible for translating, manufacturing, marketing, and selling a set of books in its country. Part of your responsibilities is interfacing with managers in each of the divisions in your region (Central and South America), overseeing their budgeting and financial reporting to headquarters, and leading a virtual team consisting of the top managers in charge of each of the divisions in your region. The virtual team's mission is to promote

global learning, explore new potential opportunities and markets, and address ongoing problems. You communicate directly with division managers via telephone and email, as well as written reports, memos, and faxes. When virtual team meetings are convened, videoconferencing is often used.

After your first few virtual team meetings, you noticed that the managers seemed to be reticent about speaking up. Interestingly enough, when each manager communicates with you individually, primarily in telephone conversations, she or he tends to be very forthcoming and frank and you feel you have a good rapport with each of them. However, getting the managers to communi-

cate with one another as a virtual team has been a real challenge. At the last meeting, you tried to prompt some of the managers to raise issues relevant to the agenda that you knew was on their minds from your individual conversations with them. Surprisingly, the managers skillfully avoided informing their teammates about the heart of the issues in question. You are confused and troubled. While you feel your other responsibilities are going well, you know that your virtual team is not operating like a team at all, and no matter what you try, discussions in virtual team meetings are forced and generally unproductive. What are you going to do to address this problem?



Additional Activities on the Build Your Management Skills DVD

- **Self-Assessment:** Team Roles Preference Scale
- **Manager's Hot Seat:** Working in Teams: Cross-Functional Dysfunction

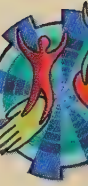
Managing Ethically

Some self-managed teams encounter a vexing problem: One or more members engage in social loafing, and other members are reluctant to try to rectify the situation. Social loafing can be especially troubling if team members' pay is based on team performance and social loafing reduces the team's performance and thus the pay of all members (even the highest per-

formers). Even if managers are aware of the problem, they may be reluctant to take action because the team is supposedly self-managing.

Questions

1. Either individually or in a group, think about the ethical implications of social loafing in a self-managed team.
2. Do managers have an ethical obligation to step in when they are aware of social loafing in a self-managed team? Why or why not? Do other team members have an obligation to try to curtail the social loafing? Why or why not?



Case for Discussion

Teams Excel at Louis Vuitton and Nucor Corporation

How can managers use teams in different kinds of organizations and work environments to gain a competitive advantage?

Groups and teams are relied on in all kinds of organizations, from those specializing in heavy industrial manufacturing to those in high-tech fields ranging from computer software development to biotechnology. Relying on groups and teams to accomplish work tasks is one thing; managing groups and teams in ways that enable them to truly excel and help an organization gain and maintain a competitive advantage is another, much more challenging endeavor. Managers at Louis Vuitton, the most profitable luxury brand in the world, and managers at Nucor Corporation, the largest producer of steel and biggest recycler in the United States, have succeeded in effectively using teams to produce luxury accessories and steel, respectively. Teams at both companies not only are effective but truly excel and have helped to make the companies leaders in their respective industries.⁷¹

Louis Vuitton is the largest and most profitable producer of high-

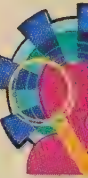
end luxury accessories.⁷² Impeccable quality and high standards are a must for Louis Vuitton; when customers purchase a handbag such as the Boulogne Multicolor, which appeared in stores for the first time in March 2004 with a \$1,500 price tag, they expect only the best. Teams at Louis Vuitton are so effective at making handbags and other accessories that not only are customers never disappointed but Vuitton's profit margins are much higher than those of its competitors such as Prada and Gucci.⁷³

Teams with between 20 and 30 members make Vuitton handbags and accessories. The teams work on only one particular product at a time; a team with 24 members might produce about 120 handbags per day. Team members are empowered to take ownership for the goods they produce, are encouraged to suggest improvements, and are kept up to date on key facts such as products' selling prices and popularity. As Thierry Nogues, a team leader at a Vuitton factory in Ducey, France, puts it, "Our goal is to make everyone as multiskilled and autonomous as possible."⁷⁴

In the case of the Boulogne Multicolor, a team found out that some of the studs on the handbag were interfering with the smooth operation of the zipper. The team's discovery led to a small design change that completely eliminated the problem.⁷⁵ By being involved in all aspects of the goods they produce, and having the skills and autonomy to ensure that all goods produced live up to the Vuitton brand name, employees take pride in their work and are highly motivated.

Headquartered in Charlotte, North Carolina, Nucor has operations in 14 states, manufacturing all kinds of steel products ranging from steel joists, bars, and beams to steel decks and metal building systems.⁷⁶ Nucor has over 9,900 employees and over \$6.2 billion in annual sales.⁷⁷

Production workers at Nucor are organized into teams ranging in size from 8 to 40 members based on the kind of work the team is responsible for, such as rolling steel or operating a furnace. Team members have considerable autonomy to make decisions and creatively respond to problems and



opportunities, and there are relatively few layers in the corporate hierarchy supporting the empowerment of teams.⁷⁸ Teams develop their own informal rules for behavior and make their own decisions. As long as team members follow organizational rules and policies (e.g., for safety) and meet quality standards, they are free to govern themselves. Managers act as coaches or advisers rather than supervisors, helping teams out when they need some additional outside assistance.⁷⁹

To ensure that production teams are motivated to help Nucor achieve its goals, team members are eligible for weekly bonuses based on the team's performance. Essentially, these production workers receive base pay that does not vary and are eligible to receive weekly bonus pay that can average from 80 to 150 percent of their regular pay.⁸⁰ The bonus rate is predetermined by the work a team performs and the ca-

pabilities of the machinery they use. Given the immediacy of the bonus and its potential magnitude, team members are highly motivated to perform at a high level, develop informal rules that support high performance, and strive to help Nucor reach its goals. Moreover, because all members of a team receive the same amount of weekly bonus money, they are motivated to do their best for the team, cooperate, and help one another out.⁸¹

Crafting a luxury handbag and making steel joists couldn't be more different from each other in certain ways. Yet the highly effective teams at Louis Vuitton and Nucor share certain fundamental qualities. These teams really do take ownership of their work and are highly motivated to perform effectively. Team members have the skills and knowledge they need to be effective, they are empowered to make decisions about their work, and they know that their teams are

making vital contributions to their organizations.⁸²

Questions

1. Why are workers at Louis Vuitton and Nucor highly motivated?
2. What are the key ingredients for the successful use of self-managed teams at Louis Vuitton and Nucor?
3. How do managers at these two companies ensure that team members are highly motivated, work well together, and make meaningful contributions to their teams and the company as a whole?
4. Could other companies adopt the approach of Louis Vuitton and Nucor in their manufacturing facilities? Why or why not?

Shaking Up Intel's Insides

Long before announcing a sweeping reorganization of Intel Corp.'s operating divisions on Jan. 17, CEO-designate Paul S. Otellini had been telling the world about a major shift in the chip-maker's strategy. Gone were the days, he said, when the company could get by with a single-minded focus on microprocessor design. Intel would instead focus more on bringing together chips and software into so-called platforms designed to perform specific tasks, such as showing movies on home PCs or keeping corporate computers virus-free. "For the first three decades of the company, we made mostly discrete chips. But they

weren't designed to be used together . . . and they weren't marketed together," Otellini told *BusinessWeek* in November.

Now he's making it clear to employees that, under his leadership, Intel truly is entering a new era. Otellini, who officially takes the helm on May 18, will be the first chief executive without an engineering degree at a company where gearheads have reigned supreme. He believes that to keep Intel growing, every idea and technical solution should be focused on meeting customers' needs from the outset. So rather than relying on its engineering prowess, Intel's reorganization will bring together engi-

neers, software writers, and marketers into five market-focused units: corporate computing, the digital home, mobile computing, health care, and channel products—PCs for small manufacturers.

The reorganization is not without challenges, but if Otellini succeeds it will amount to a revolution. For years, Intel has built one-size-fits-all processors, then expected customers to adopt them in various markets. But tech companies increasingly are being asked to deliver solutions that respond to the end user's demands. Corporations, for instance, are looking to prevent their systems from crashing, but employees frequent sites that

contain viruses or spyware. Intel has responded by developing chips and software that quarantine these PCs and limit the damage.

Tandem Approach

Otellini's reorganization is supposed to ensure that such product tailoring becomes part of Intel's DNA. How will it work? The company's Centrino wireless notebook platform provides some clues. Intel first determined consumers wanted a powerful notebook with decent battery life that connected wirelessly to the Net. Armed with this knowledge, engineers and software writers designed a package of chips that would do that. Later, engineers and marketing people joined forces to create advertising that would persuade consumers to pay a premium for Centrino-powered notebooks. It worked: As of December, Intel had 87 percent of the notebook PC market, says Mercury Research.

But imposing such a management structure across the company won't be easy. For one thing, Otellini has taken the unusual step of putting two execs apiece in charge of the two biggest groups, mobility and corporate computing. Intel has used this "two-men-in-a-box" approach before, but it will be particularly tricky under the new structure. Each unit will be responsible for several market segments; for example, the mobility unit will build platforms for notebooks, handhelds, and cell phones. So divvying up each co-chief's duties will be a challenge. Getting that right is crucial or the rank and file won't know who to report to.

The new regime will cause a jolt to the culture. For decades, employees have been compensated for their own work. Now teams will be judged as a whole. Engineers, long the top dogs, may resist working with others. "It's like saying to a baseball player, 'Gee, we're decid-

ing to play pro football,'" says Edward E. Lawler, a professor at USC's Marshall School of Business. "All of a sudden, the rules of the game are very different."

Otellini has begun to put the pieces in place. Now he'll need the teamwork of his people to pull it off.

Questions

1. Why did Paul Otellini reorganize Intel?
2. What are the advantages of having co-chiefs oversee large groups?
3. Why is it important that team members (including engineers) work well together?
4. Why are teams being judged as a whole?

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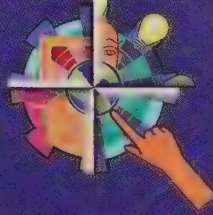
CHAPTER 12

Building and Managing Human Resources

Learning Objectives

After studying this chapter, you should be able to:

- Explain why strategic human resource management can help an organization gain a competitive advantage.
- Describe the steps managers take to recruit and select organizational members.
- Discuss the training and development options that ensure organizational members can effectively perform their jobs.
- Explain why performance appraisal and feedback is such a crucial activity.
- Explain the issues managers face in determining levels of pay and benefits.



Management Snapshot

Effectively Managing Human Resources at Semco

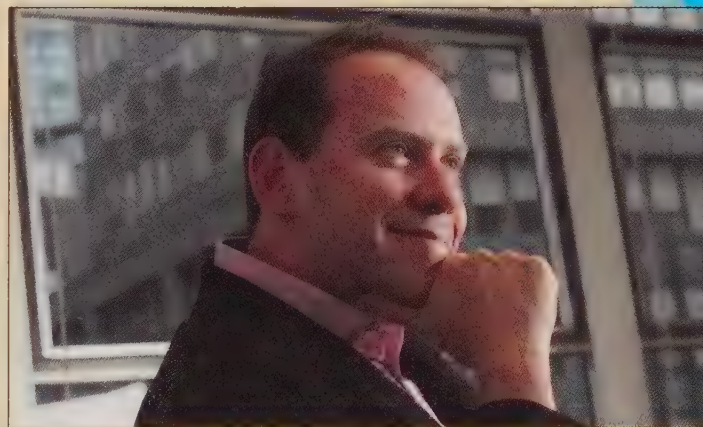
How can managers provide employees with freedom and flexibility at work while ensuring their companies' growth and profitability?

Ricardo Semler was 21 years old when he took his father's place as head of the family business, Semco, based in Sao Paulo, Brazil, in 1984.¹ Today, Semco's revenues are over \$200 million a year from a diverse set of businesses ranging from industrial machinery and facility management to environmental consulting and Web-based HRM outsourcing. In addition to growing over 30 percent a year and generating its own cash to support this growth (Semco is a private company), Semco is very profitable.²

Semler is the first to admit that Semco's phenomenal success is due to its human resources—its employees. In fact, Semler so firmly believes in Semco's employees that he and other top managers at Semco are reluctant to tell employees what to do. Semco has no rules, regulations, or organizational charts; workplace democracy rules the day. Employees have levels of autonomy unheard of in

other companies, and flexibility and trust are built into every aspect of human resource management at Semco.³

Human resource practices at Semco revolve around maximizing the contributions employees make to the company, and this begins by hiring individuals who want, can, and will contribute. Semco strives to ensure that all selection decisions are made based on



Ricardo Semler believes in treating employees like adults.

relevant and complete information. Job candidates meet many employees, receive a tour of the company, and interact with potential co-workers. Once finalists are identified from the pool, multiple Semco employees interview

them five or six more times to choose the best person(s) to be hired. The result is that both Semco and new hires make very informed decisions and are mutually committed to making the relation a success.⁴

Once hired, entry-level employees rotate through different positions and units of their own choosing for about a year.⁵ In this way, the new hires learn about their options and can decide where their interests lie, and the units they work in learn about the new hires. At the end of the year, the new employees may be offered a job in one of the units in which they worked, or they may seek a position elsewhere in Semco. Seasoned Semco employees are also encouraged to rotate positions and work in different parts of the company.⁶

Employees at Semco are free to choose when and where they work.⁷ Semler realizes that employees have lives outside the workplace and gives them the freedom to manage their work and free time; Semler does not expect them to work excessive hours either. What is expected of all employees and all units at Semco is performance.⁸

Performance is appraised at Semco in terms of results. Every six months, all busi-

ness units are required to demonstrate that their continued operation is producing value for Semco and its customers. Similarly, all employees and managers must demonstrate that they are making valuable contributions. For example, each manager's performance is anonymously appraised by all of the employees who report to him or her.⁹

Employees can choose how they are paid from a combination of 11 different compensation options. Flexibility in compensation promotes risk taking and innovation, according to Semler, and maximizes returns to employees in the form of their pay and to the company in terms of revenues and profitability.¹⁰

Flexibility, autonomy, the ability to change jobs often, and control of working hours and even compensation are some of the ways by which Semler strives to ensure that employees are involved in their work because they *want* to be; turnover at Semco is less than 1 percent annually.¹¹ And with human resource practices geared toward maximizing contributions and performance, Semco is well poised to continue to provide value to its customers.

Overview

Managers are responsible for acquiring, developing, protecting, and utilizing the resources that an organization needs to be efficient and effective. One of the most important resources in all organizations is human resources—the people involved in the production and distribution of goods and services. Human resources include all members of an organization, ranging from top managers to entry-level employees. Effective managers like Ricardo Semler in the “Management Snapshot” realize how valuable human resources are and take active steps to make sure that their organizations build and fully utilize their human resources to gain a competitive advantage.

This chapter examines how managers can tailor their human resource management system to their organization's strategy and structure. We discuss in particular the major components of human resource management: recruitment and selection, training and development, performance appraisal, pay and benefits, and labor relations. By the end of this chapter, you will understand the central role human resource management plays in creating a high-performing organization.

Strategic Human Resource Management

human resource management

Activities that managers engage in to attract and retain employees and to ensure that they perform at a high level and contribute to the accomplishment of organizational goals.

strategic human resource management

The process by which managers design the components of a human resource management system to be consistent with each other, with other elements of organizational architecture, and with the organization's strategy and goals.

Human resource management (HRM) includes all the activities managers engage in to attract and retain employees and to ensure that they perform at a high level and contribute to the accomplishment of organizational goals. These activities make up an organization's human resource management system, which has five major components: recruitment and selection, training and development, performance appraisal and feedback, pay and benefits, and labor relations (see Figure 12.1).

Strategic human resource management is the process by which managers design the components of an HRM system to be consistent with each other, with other elements of organizational architecture, and with the organization's strategy and goals.¹² The objective of strategic HRM is the development of an HRM system that enhances an organization's efficiency, quality, innovation, and responsiveness to customers—the four building blocks of competitive advantage. At Semco in the "Management Snapshot," HRM practices ensure that employees make meaningful contributions, are innovative, are efficient, and provide value to customers.

As part of strategic human resource management, some managers have adopted "Six Sigma" quality improvement plans. These plans ensure that an organization's products and services are as free of error or defects as possible through a variety of human resource-related initiatives. Jack Welch, former CEO of General Electric Company, has indicated that these initiatives have saved his company millions of dollars, and other companies, such as Whirlpool and Motorola, also have implemented Six Sigma initiatives. In order for such initiatives to be effective, however, top managers have to be committed to Six Sigma, employees must be motivated, and there must be demand for the products or services of the organization in the first place. David Fitzpatrick, head of Deloitte Consulting's Lean Enterprise Practice, estimates that most Six Sigma plans are not effective because the conditions for

Figure 12.1

Components of a Human Resource Management System



Each component of an HRM system influences the others, and all five must fit together

effective Six Sigma are not in place. For example, if top managers are not committed to the quality initiative, they may not devote the necessary time and resources to make it work and may lose interest in it prematurely.¹³

Overview of the components of HRM

Managers use *recruitment and selection*, the first component of an HRM system, to attract and hire new employees who have the abilities, skills, and experiences that will help an organization achieve its goals. Microsoft Corporation, for example, has the goal of remaining the premier computer software company in the world. To achieve this goal, Bill Gates realizes the importance of hiring only the best software designers. When Microsoft hires new software designers, hundreds of highly qualified candidates with excellent recommendations are interviewed and rigorously tested; only the very best are hired. This careful attention to selection has contributed to Microsoft's competitive advantage. Microsoft has little trouble recruiting top programmers because candidates know they will be at the forefront of the industry if they work for Microsoft, utilizing the latest technology and working with the best people.¹⁴

After recruiting and selecting employees, managers use the second component, *training and development*, to ensure that organizational members develop the skills and abilities that will enable them to perform their jobs effectively in the present and the future. Training and development is an ongoing process; changes in technology and the environment, as well as in an organization's goals and strategies, often require that organizational members learn new techniques and ways of working. At Microsoft Corporation, newly hired program designers receive on-the-job training by joining small teams that include experienced employees who serve as mentors or advisers. New recruits learn firsthand from team members how to go about developing computer systems that are responsive to customers' programming needs.¹⁵

The third component, *performance appraisal and feedback*, serves two different purposes in HRM. First, performance appraisal can provide managers with the information they need to make good human resources decisions—decisions about how to train, motivate, and reward organizational members.¹⁶ Second, feedback from performance appraisal serves a developmental purpose for members of an organization. When managers regularly evaluate their subordinates' performance, they can provide employees with valuable information about their strengths and weaknesses and the areas in which they need to concentrate.

On the basis of performance appraisals, managers distribute *pay* to employees, part of the fourth component of an HRM system. By rewarding high-performing organizational members with pay raises, bonuses, and the like, managers increase the likelihood that an organization's most valued human resources are motivated to continue their high levels of contribution to the organization. Moreover, by linking pay to performance, high-performing employees are more likely to stay with the organization, and managers are more likely to fill positions that become open with highly talented individuals. *Benefits* such as health insurance are important outcomes that employees receive by virtue of their membership in an organization.

Last, but not least, *labor relations* encompass the steps that managers take to develop and maintain good working relationships with the labor unions that may represent their employees' interests. For example, an organization's labor relations

component can help managers establish safe working conditions and fair labor practices in their offices and plants.

Managers must ensure that all five of these components fit together and complement their company's structure and control systems.¹⁷ For example, if managers decide to decentralize authority and empower employees, they need to invest in training and development to ensure that lower-level employees have the knowledge and expertise they need to make the decisions that top managers would make in a more centralized structure.

Each of the five components of HRM influences the others (see Figure 12.1).¹⁸ The kinds of people that the organization attracts and hires through recruitment and selection, for example, determine (1) the kinds of training and development that are necessary, (2) the way performance is appraised, and (3) the appropriate levels of pay and benefits. Managers at Microsoft ensure that their organization has highly qualified program designers by (1) recruiting and selecting the best candidates, (2) providing new hires with the guidance of experienced team members so that they learn how to be responsive to customers' needs when designing programs and systems, (3) appraising program designers' performance in terms of their individual contributions and their team's performance, and (4) basing programmers' pay on individual and team performance.

The legal environment of HRM

In the rest of this chapter we focus in detail on the choices managers must make in strategically managing human resources to attain organizational goals and gain a competitive advantage. Effectively managing human resources is a complex undertaking for managers, and we provide an overview of some of the major issues they face. Before we do, however, we need to look at how the legal environment affects human resource management.

The local, state, and national laws and regulations that managers and organizations must abide by add to the complexity of HRM. For example, the U.S. government's commitment to **equal employment opportunity (EEO)** has resulted in the creation and enforcement of a number of laws that managers must abide by. The goal of EEO is to ensure that all citizens have an equal opportunity to obtain employment regardless of their gender, race, country of origin, religion, age, or disabilities. Table 12.1 summarizes some of the major EEO laws affecting HRM. Other laws, such as the Occupational Safety and Health Act of 1970, require that managers ensure that employees are protected from workplace hazards and safety standards are met.

In Chapter 3, we explained how effectively managing diversity is an ethical and business imperative and discussed the many issues surrounding diversity. EEO laws and their enforcement make the effective management of diversity a legal imperative as well. The Equal Employment Opportunity Commission (EEOC) is the division of the Department of Justice that enforces most of the EEO laws and handles discrimination complaints. In addition, the EEOC issues guidelines for managers to follow to ensure that they are abiding by EEO laws. For example, the Uniform Guidelines on Employee Selection Procedures issued by the EEOC (in conjunction with the Departments of Labor and Justice and the Civil Service Commission) provide managers with guidance on how to ensure that the recruitment and selection component of human resource management complies with Title VII of the Civil Rights Act (which prohibits discrimination based on gender, race, color, religion, and national origin).¹⁹

equal employment opportunity

The equal right of all citizens to have the opportunity to obtain employment regardless of their gender, age, race, country of origin, religion, or disabilities.

Table 12.1**Major Equal Employment Opportunity Laws Affecting HRM**

Year	Law	Description
1963	Equal Pay Act	Requires that men and women be paid equally if they are performing equal work
1964	Title VII of the Civil Rights Act	Prohibits discrimination in employment decisions on the basis of race, religion, sex, color, or national origin; covers a wide range of employment decisions, including hiring, firing, pay, promotion, and working conditions
1967	Age Discrimination in Employment Act	Prohibits discrimination against workers over the age of 40 and restricts mandatory retirement
1978	Pregnancy Discrimination Act	Prohibits discrimination against women in employment decisions on the basis of pregnancy, childbirth, and related medical decisions
1990	Americans with Disabilities Act	Prohibits discrimination against individuals with disabilities in employment decisions and requires that employers make accommodations for such workers to enable them to perform their jobs
1991	Civil Rights Act	Prohibits discrimination (as does Title VII) and allows for the awarding of punitive and compensatory damages, in addition to back pay, in cases of intentional discrimination
1993	Family and Medical Leave Act	Requires that employers provide 12 weeks of unpaid leave for medical and family reasons, including paternity and illness of a family member

Contemporary challenges that managers face related to the legal environment include how to eliminate sexual harassment (see Chapter 3 for an in-depth discussion of sexual harassment), how to make accommodations for employees with disabilities, how to deal with employees who have substance-abuse problems, and how to manage HIV-positive employees and employees with AIDS.²⁰ HIV-positive employees are infected with the virus that causes AIDS but may show no AIDS symptoms and may not develop AIDS in the near future. Often, such employees are able to perform their jobs effectively, and managers must take steps to ensure that they are allowed to do so and are not discriminated against in the workplace.²¹ Employees with AIDS may or may not be able to perform their jobs effectively, and, once again, managers need to ensure that they are not unfairly discriminated against.²² Many organizations have instituted AIDS awareness training programs to educate organizational members about HIV and AIDS, dispel unfounded myths about how HIV is spread, and ensure that individuals infected with the HIV virus are treated fairly and are able to be productive as long as they can be while not putting others at risk.²³

recruitment

Activities that managers engage in to develop a pool of qualified candidates for open positions.

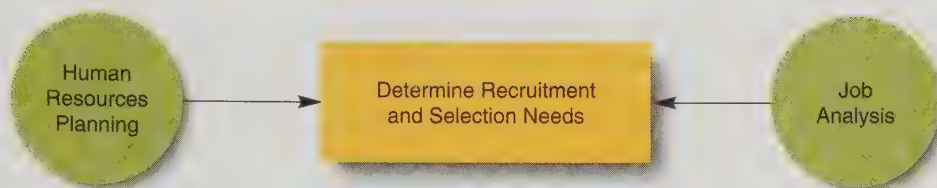
selection

The process that managers use to determine the relative qualifications of job applicants and their potential for performing well in a particular job.

Recruitment and Selection

Recruitment includes all the activities managers engage in to develop a pool of qualified candidates for open positions.²⁴ **Selection** is the process by which managers determine the relative qualifications of job applicants and their

Figure 12.2
The Recruitment and Selection System



potential for performing well in a particular job. Prior to actually recruiting and selecting employees, managers need to engage in two important activities: human resource planning and job analysis (Figure 12.2).

Human resource planning

human resource planning Activities that managers engage in to forecast their current and future needs for human resources.

Human resource planning includes all the activities managers engage in to forecast their current and future human resource needs. Current human resources are the employees an organization needs today to provide high-quality goods and services to customers. Future human resource needs are the employees the organization will need at some later date to achieve its longer-term goals.

As part of human resource planning, managers must make both demand forecasts and supply forecasts. *Demand forecasts* estimate the qualifications and numbers of employees an organization will need given its goals and strategies. *Supply forecasts* estimate the availability and qualifications of current employees now and in the future, as well as the supply of qualified workers in the external labor market.

As a result of their human resource planning, managers sometimes decide to **outsource** to fill some of their human resource needs. Instead of recruiting and selecting employees to produce goods and services, managers contract with people who are not members of their organization to produce goods and services. Managers in publishing companies, for example, frequently contract with freelance editors to copyedit new books that they intend to publish. Kelly Services is an organization that provides temporary typing, clerical, and secretarial workers to managers who want to use outsourcing to fill some of their human resource requirements in these areas.

Two reasons why human resource planning sometimes leads managers to outsource are flexibility and cost. First, outsourcing can give managers increased flexibility, especially when accurately forecasting human resource needs is difficult, human resource needs fluctuate over time, or finding skilled workers in a particular area is difficult. Second, outsourcing can sometimes allow managers to make use of human resources at a lower *cost*. When work is outsourced, costs can be lower for a number of reasons: The organization does not have to provide benefits to workers; managers are able to contract for work only when the work is needed; and managers do not have to invest in training. Outsourcing can be used for functional activities such as after-sales service on appliances and equipment, legal work, and the management of information systems. Roy Richie, general counsel for the Chrysler Corporation, uses temporary attorneys to write contracts and fill some of his department's human resource needs. As he says, "The math works. . . . Savings can be tremendous."²⁵

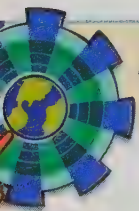
Outsourcing does have its disadvantages, however. When work is outsourced, managers may lose some control over the quality of goods and services. Also, individuals performing outsourced work may have less knowledge of organizational practices, procedures, and goals and less commitment to an organization than

outsource To use outside suppliers and manufacturers to produce goods and services.

regular employees. In addition, unions resist outsourcing because it has the potential to eliminate some of their members. To gain some of the flexibility and cost savings of outsourcing and avoid some of outsourcing's disadvantages, a number of organizations, such as Microsoft and IBM, rely on a pool of temporary employees to, for example, debug programs.

A major trend reflecting the increasing globalization of business is the outsourcing of office work, computer programming, and technical jobs from the United States and countries in western Europe, with high labor costs, to countries like India and China, with low labor costs.²⁶ For example, computer programmers in India and China earn a fraction of what their U.S. counterparts earn. In 2003, India alone provided over \$9 billion worth of software and technological outsourcing services to companies in North America, western Europe, Latin America, Asia and the Pacific Rim, and Japan; North American companies accounted for the majority of outsourcing to India.²⁷

As companies gain experience in outsourcing software and technological services, managers are learning what kinds of work can be effectively outsourced and what work should probably not be outsourced. In India, for example, the workforce is highly trained and motivated, and cities like Bangalore are bustling with high-tech jobs and companies like Infosys Technologies are providing software services to companies abroad. Managers who have outsourcing experience have found that outsourcing works best for tasks that can be rule-based, do not require closeness/familiarity with customers and/or the customs and culture of the country in which the company is based, and do not require creativity.²⁸ When the work requires the recognition and solution of problems rather than the application of preexisting algorithms, creativity in developing solutions, and independent thinking and judgment without the guidance of standard operating procedures, performance might suffer from outsourcing. Essentially, the more complex and uncertain the work and the more it depends on being close to customers and the company itself, the less advantageous outsourcing tends to be.²⁹ As indicated in the following "Managing Globally," these trade-offs between gaining the cost advantages of outsourcing and being responsive to customers, providing effective services, and developing innovative products have led some managers to cease outsourcing certain kinds of tasks that might be better performed by an organization's own employees.³⁰



Managing Globally

When Outsourcing Doesn't Make Sense

Hermant Kurande, one of the founders of Storability Software in Southborough, Massachusetts, and head of technology at the firm, started outsourcing three years ago. He outsourced software programming work to India, where labor costs were about 25 percent of what they would have been if the work were performed in-house. Storability tried different approaches to effectively utilize low-cost Indian labor for its programming tasks, but after experiencing a number of problems, it decided to hire more programmers and now does most of its programming in the United States. While Kurande was born and educated in India and received his master's degree from the Indian Institute of Technology in Bombay, he found that the "depth of knowledge in the area we want to build software is not good enough among Indian programmers."³¹

Dey Ittycheria, also born in India and CEO of Bladelogic, which develops network management software in Waltham, Massachusetts, has faced similar challenges in his efforts to outsource programming to India. Bladelogic, whose customers include General Electric and Sprint, started outsourcing in 2001, soon after the company was founded. Even though the labor costs in India were 35 percent of what they would have been in the United States, Ittycheria found that it actually cost more to outsource work to India when he took into account productivity; as a result, most of Bladelogic's programming work is now done by its own employees in the United States.³² Ittycheria and Kurande are not alone in their disenchantment with outsourcing programming. According to Nariman Bahravish, an economist with the consulting and forecasting firm Global Insight, "Only certain kinds of tasks can be outsourced—what can be set down as a set of rules . . . that which requires more creativity is more difficult to manage at a distance."³³

Nonetheless, there are many kinds of tasks that can be effectively outsourced, and the cost savings for these tasks can be considerable. And some managers believe that many programming tasks can be effectively outsourced as well, even those requiring creativity. For example, according to Bassab Pradham, vice president for worldwide sales at Infosys Technologies, based in Bangalore, India, Infosys effectively provided over \$700 million worth of data entry, programming, and technical support services to major North American companies like Cisco Systems, Visa International, and Boeing in 2003. However, Pradham does concede that "whenever the pace of innovation is very rapid . . . the work should be done closer to the client."³⁴ All in all, estimates from researchers studying workplace trends, such as the Cato Institute in Washington, DC, project that companies in the United States will continue to increase their utilization of outsourcing to lower costs in the next decade.³⁵ More generally, analysts estimate that the outsourcing industry grew by over 30 percent in 2005.³⁶ Clearly, though, managers need to carefully determine which tasks can be effectively outsourced and which can be better performed closer to home.³⁷

Job analysis

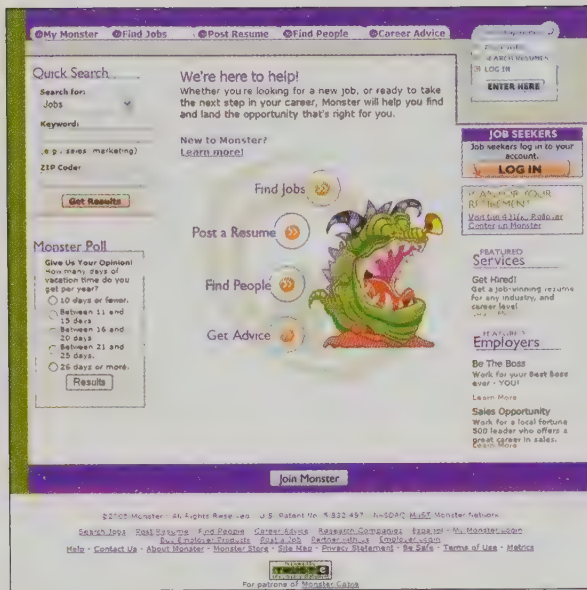
job analysis

Identifying the tasks, duties, and responsibilities that make up a job and the knowledge, skills, and abilities needed to perform the job.

Job analysis is a second important activity that managers need to undertake prior to recruitment and selection.³⁸ **Job analysis** is the process of identifying (1) the tasks, duties, and responsibilities that make up a job (the *job description*), and (2) the knowledge, skills, and abilities needed to perform the job (the *job specifications*).³⁹ For each job in an organization, a job analysis needs to be done.

A job analysis can be done in a number of ways, including observing current employees as they perform the job or interviewing them. Often, managers rely on questionnaires compiled by jobholders and their managers. The questionnaires ask about the skills and abilities needed to perform the job, job tasks and the amount of time spent on them, responsibilities, supervisory activities, equipment used, reports prepared, and decisions made.⁴⁰ A trend, in some organizations, is toward more flexible jobs in which tasks and responsibilities change and cannot be clearly specified in advance. For these kinds of jobs, job analysis focuses more on determining the skills and knowledge workers need to be effective and less on specific duties.

After managers have completed human resource planning and job analyses for all jobs in an organization, they will know their human resource needs and the jobs



Employment Web sites like www.monster.com are becoming an increasingly popular external recruitment tool. One advantage of such Web sites is that they can reach out to a broader applicant pool and can even be used to fill global positions.

Many large organizations send teams of interviewers to college campuses to recruit new employees. External recruitment can also take place through informal networks, as occurs when current employees inform friends about open positions in their companies or recommend people they know to fill vacant spots. Some organizations use employment agencies for external recruitment, and some external recruitment takes place simply through walk-ins—job hunters coming to an organization and inquiring about employment possibilities.

With all the downsizings and corporate layoffs that have taken place in recent years, you might think that external recruiting would be a relatively easy task for managers. However, it often is not, because even though many people may be looking for jobs, many of the jobs that are opening up require skills and abilities that these job hunters do not have. Managers needing to fill vacant positions and job hunters seeking employment opportunities are increasingly relying on the Web to make connections with each other through employment Web sites such as Monster.com⁴² and Jobline International, Europe's largest electronic recruiting site, with operations in 12 countries.⁴³ Major corporations such as Coca-Cola, Cisco, Ernst & Young, Canon, and Telia have relied on Jobline to fill global positions.⁴⁴

External recruiting has both advantages and disadvantages for managers. Advantages include having access to a potentially large applicant pool; being able to attract people who have the skills, knowledge, and abilities that an organization needs to achieve its goals; and being able to bring in newcomers who may have a fresh approach to problems and be up to date on the latest technology. These advantages have to be weighed against the disadvantages, including the relatively high costs of external recruitment. Employees recruited externally also lack knowledge about the inner workings of the organization and may need to receive more

they need to fill. They will also know the knowledge, skills, and abilities that potential employees need to perform those jobs. At this point, recruitment and selection can begin.

External and internal recruitment

As noted earlier, recruitment is what managers do to develop a pool of qualified candidates for open positions.⁴¹ They traditionally have used two main types of recruiting: external and internal, which is now supplemented by recruiting over the Internet.

EXTERNAL RECRUITING When managers recruit externally to fill open positions, they look outside the organization for people who have not worked for the organization previously. There are multiple means through which managers can recruit externally—advertisements in newspapers and magazines, open houses for students and career counselors at high schools and colleges or on-site at the organization, career fairs at colleges, and recruitment meetings with groups in the local community.

training than those recruited internally. Finally, when employees are recruited externally, there is always uncertainty concerning whether they will actually be good performers.

lateral move A job change that entails no major changes in responsibility or authority levels.

INTERNAL RECRUITING When recruiting is internal, managers turn to existing employees to fill open positions. Employees recruited internally are either seeking **lateral moves** (job changes that entail no major changes in responsibility or authority levels) or promotions. Internal recruiting has several advantages. First, internal applicants are already familiar with the organization (including its goals, structure, culture, rules, and norms). Second, managers already know candidates; they have considerable information about their skills and abilities and actual behavior on the job. Third, internal recruiting can help boost levels of employee motivation and morale, both for the employee who gets the job and for other workers. Those who are not seeking a promotion or who may not be ready for one can see that promotion is a possibility for the future; or a lateral move can alleviate boredom once a job has been fully mastered and can also be a useful way to learn new skills. Finally, internal recruiting is normally less time-consuming and expensive than external recruiting.

Given the advantages of internal recruiting, why do managers rely on external recruiting as much as they do? The answer is because of the disadvantages of internal recruiting—among them, a limited pool of candidates and a tendency among those candidates to be set in the organization's ways. Often, the organization simply does not have suitable internal candidates. Sometimes, even when suitable internal applicants are available, managers may rely on external recruiting to find the very best candidate or to help bring new ideas and approaches into their organization. When organizations are in trouble and performing poorly, external recruiting is often relied on to bring in managerial talent with a fresh approach. For example, when IBM's performance was suffering in the 1990s and the board of directors was looking for a new CEO, rather than consider any of IBM's existing top managers for this position, the board recruited Lou Gerstner, an outsider who had no previous experience in the computer industry.

The selection process

Once managers develop a pool of applicants for open positions through the recruitment process, they need to find out whether each applicant is qualified for the position and likely to be a good performer. If more than one applicant meets these two conditions, managers must further determine which applicants are likely to be better performers than others. They have several selection tools to help them sort out the relative qualifications of job applicants and appraise their potential for being good performers in a particular job. These tools include background information, interviews, paper-and-pencil tests, physical ability tests, performance tests, and references (see Figure 12.3).⁴⁵

BACKGROUND INFORMATION To aid in the selection process, managers obtain background information from job applications and from résumés. Such information might include the highest levels of education obtained, college majors and minors, type of college or university attended, years and type of work experience, and mastery of foreign languages. Background information can be helpful both to screen out applicants who are lacking key qualifications (such as a college

Figure 12.3
Selection Tools



degree) and to determine which qualified applicants are more promising than others. For example, applicants with a BS may be acceptable, but those who also have an MBA are preferable.

INTERVIEWS Virtually all organizations use interviews during the selection process. Interviews may be structured or unstructured. In a *structured interview*, managers ask each applicant the same standard questions (e.g., “What are your unique qualifications for this position?” and “What characteristics of a job are most important for you?”). Particularly informative questions may be those that prompt an interviewee to demonstrate skills and abilities needed for the job by answering the question. Sometimes called *situational interview questions*, these often present interviewees with a scenario that they would likely encounter on the job and ask them to indicate how they would handle it.⁴⁶ For example, applicants for a sales job may be asked to indicate how they would respond to a customer who complains about waiting too long for service, a customer who is indecisive, and a customer whose order is lost.

An *unstructured interview* proceeds more like an ordinary conversation. The interviewer feels free to ask probing questions to discover what the applicant is like and does not ask a fixed set of questions determined in advance. In general, structured interviews are superior to unstructured interviews because they are more likely to yield information that will help identify qualified candidates and are less subjective. Also, evaluations based on structured interviews may be less influenced by the interviewer’s biases than evaluations based on unstructured interviews.

When conducting interviews, managers cannot ask questions that are irrelevant to the job in question; otherwise, their organizations run the risk of costly lawsuits. It is inappropriate and illegal, for example, to inquire about an interviewee’s spouse or to ask questions about whether an interviewee plans to have children. Because questions such as these are irrelevant to job performance, they are discriminatory and violate EEO laws (see Table 12.1). Thus, interviewers need to be instructed in EEO laws and informed about questions that may violate those laws.

PAPER-AND-PENCIL TESTS The two main kinds of paper-and-pencil tests used for selection purposes are ability tests and personality tests. *Ability tests* assess the extent to which applicants possess the skills necessary for job performance, such as verbal comprehension or numerical skills. Autoworkers hired by General Motors, Chrysler, and Ford, for example, are typically tested for their ability to read and to do mathematics.⁴⁷

Personality tests measure personality traits and characteristics relevant to job performance. Some retail organizations, for example, give job applicants honesty tests to determine how trustworthy they are. The use of personality tests (including honesty tests) for hiring purposes is controversial. Some critics maintain that honesty tests do not really measure honesty (that is, they are not valid) and can be faked by job applicants. Before using any paper-and-pencil tests for selection purposes, managers must have sound evidence that the tests are actually good predictors of performance on the job in question. Managers who use tests without such evidence may be subject to costly discrimination lawsuits.

PHYSICAL ABILITY TESTS For jobs requiring physical abilities, such as firefighting, garbage collecting, and package delivery, managers use physical ability tests that measure physical strength and stamina as selection tools. Autoworkers are typically tested for mechanical dexterity because this physical ability is an important skill for high job performance in many auto plants.⁴⁸

PERFORMANCE TESTS *Performance tests* measure job applicants' performance on actual job tasks. Applicants for secretarial positions, for example, typically are required to complete a keyboarding test that measures how quickly and accurately they type. Applicants for middle- and top-management positions are sometimes given short-term projects to complete—projects that mirror the kinds of situations that arise in the job being filled—to assess their knowledge and problem-solving capabilities.⁴⁹

Assessment centers, first used by AT&T, take performance tests one step further. In a typical assessment center, about 10 to 15 candidates for managerial positions participate in a variety of activities over a few days. During this time they are assessed for the skills an effective manager needs—problem-solving skills, organization skills, communication skills, and conflict resolution skills. Some of the activities are performed individually; others are performed in groups. Throughout the process, current managers observe the candidates' behavior and measure performance. Summary evaluations are then used as a selection tool.

REFERENCES Applicants for many jobs are required to provide references from former employers or other knowledgeable sources (such as a college instructor or adviser) who know the applicants' skills, abilities, and other personal characteristics. These individuals are asked to provide candid information about the applicant. References are often used at the end of the selection process to confirm a decision to hire. Yet the fact that many former employers are reluctant to provide negative information in references sometimes makes it difficult to interpret what a reference is really saying about an applicant.

In fact, several recent lawsuits filed by applicants who felt that they were unfairly denigrated or had their privacy invaded by unfavorable references from former employers have caused managers to be increasingly wary of providing any negative information in a reference, even if it is accurate. For jobs in which the jobholder is responsible for the safety and lives of other people, however, failing to provide

accurate negative information in a reference does not just mean that the wrong person might get hired; it may also mean that other people's lives will be at stake.

reliability The degree to which a tool or test measures the same thing each time it is used.

validity The degree to which a tool or test measures what it purports to measure.

training Teaching organizational members how to perform their current jobs and helping them acquire the knowledge and skills they need to be effective performers.

THE IMPORTANCE OF RELIABILITY AND VALIDITY Whatever selection tools a manager uses, these tools need to be both reliable and valid. **Reliability** is the degree to which a tool or test measures the same thing each time it is administered. Scores on a selection test should be very similar if the same person is assessed with the same tool on two different days; if there is quite a bit of variability, the tool is unreliable. For interviews, determining reliability is more complex because the dynamic is personal interpretation. That is why the reliability of interviews can be increased if two or more different qualified interviewers interview the same candidate. If the interviews are reliable, the interviewers should come to similar conclusions about the interviewee's qualifications.

Validity is the degree to which a tool measures what it purports to measure—for selection tools, it is the degree to which the test predicts performance on the tasks or job in question. Does a physical ability test used to select firefighters, for example, actually predict on-the-job performance? Do assessment center ratings actually predict managerial performance? Do keyboarding tests predict secretarial performance? These are all questions of validity. Honesty tests, for example, are controversial because it is not clear that they validly predict honesty in such jobs as retailing and banking.

Managers have an ethical and legal obligation to use reliable and valid selection tools. Yet reliability and validity are matters of degree rather than all-or-nothing characteristics. Thus, managers should strive to use selection tools in such a way that they can achieve the greatest degree of reliability and validity. For ability tests of a particular skill, managers should keep up to date on the latest advances in the development of valid paper-and-pencil tests and use the test with the highest reliability and validity ratings possible for their purposes. Regarding interviews, managers can improve reliability by having more than one person interview job candidates.

Training and Development

development Building the knowledge and skills of organizational members so that they will be prepared to take on new responsibilities and challenges.

needs assessment An assessment of which employees need training or development and what types of skills or knowledge they need to acquire.

Training and development help to ensure that organizational members have the knowledge and skills needed to perform jobs effectively, take on new responsibilities, and adapt to changing conditions. **Training** primarily focuses

on teaching organizational members how to perform their current jobs and helping them acquire the knowledge and skills they need to be effective performers. **Development** focuses on building the knowledge and skills of organizational members so that they are prepared to take on new responsibilities and challenges. Training tends to be used more frequently at lower levels of an organization; development tends to be used more frequently with professionals and managers.

Before creating training and development programs, managers should perform a **needs assessment** to determine which employees need training or development and what type of skills or knowledge they need to acquire (see Figure 12.4, page 433).⁵⁰

Types of training

There are two types of training: classroom instruction and on-the-job training.

CLASSROOM INSTRUCTION Through classroom instruction, employees acquire knowledge and skills in a classroom setting. This instruction may take place

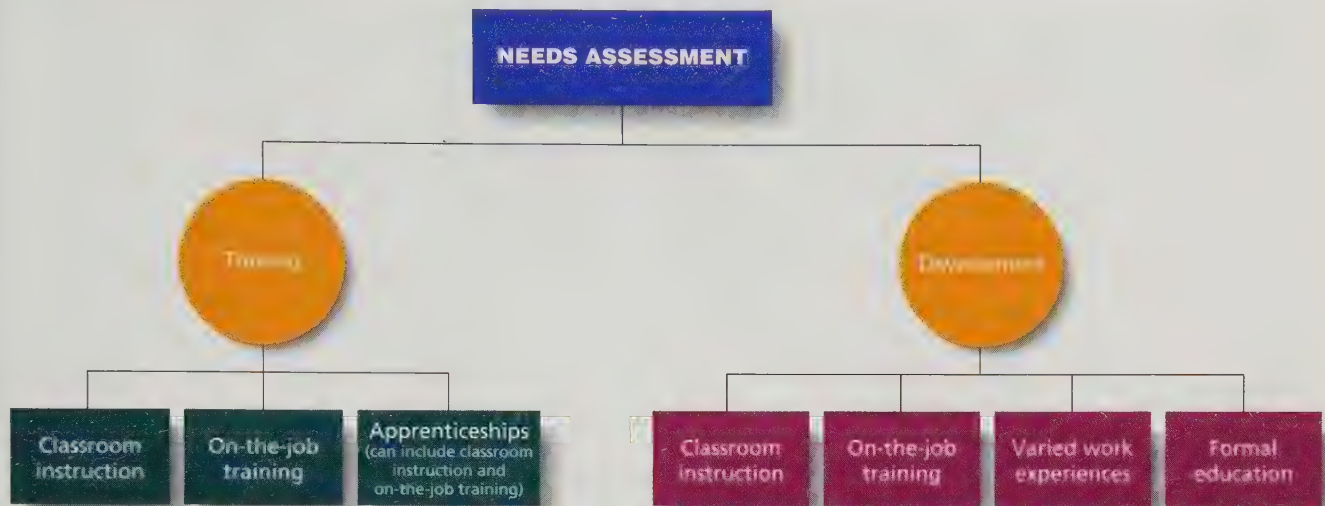


Figure 12.4
Training and Development

within the organization or outside it, such as courses at local colleges and universities. Many organizations actually establish their own formal instructional divisions—some are even called “colleges”—to provide needed classroom instruction.

Classroom instruction frequently includes the use of videos and role playing in addition to traditional written materials, lectures, and group discussions. *Videos* can be used to demonstrate appropriate and inappropriate job behaviors. For example, by watching an experienced salesperson effectively deal with a loud and angry customer in a video clip, inexperienced salespeople can develop skills in handling similar situations. During *role playing*, trainees either directly participate in or watch others perform actual job activities in a simulated setting. At McDonald’s Hamburger University, for example, role playing helps franchisees acquire the knowledge and skills they need to manage their restaurants.

Simulations also can be part of classroom instruction, particularly for complicated jobs that require an extensive amount of learning and in which errors carry a high

cost. In a simulation, key aspects of the work situation and job tasks are duplicated as closely as possible in an artificial setting. For example, air traffic controllers are trained by simulations because of the complicated nature of the work, the extensive amount of learning involved, and the very high costs of air traffic control errors.

ON-THE-JOB TRAINING In **on-the-job training**, learning occurs in the work setting as employees perform their job tasks. On-the-job training can be provided by co-workers or supervisors or can occur simply as jobholders gain experience and knowledge from doing the work. Newly hired waiters and waitresses in chains such as Red Lobster or The Olive Garden often receive on-the-job training

on-the-job training

Training that takes place in the work setting as employees perform their job tasks.



Of the various types of training available, simulations are often used for training people to perform complicated jobs, such as that of air traffic controller. Such jobs, in which errors carry a very high cost, require an extensive amount of learning.

from experienced employees. The supervisor of a new bus driver for a campus bus system may ride the bus for a week to ensure that the driver has learned the routes and follows safety procedures. Chefs learn to create new and innovative dishes by experimenting with different combinations of ingredients and cooking techniques. For all on-the-job training, employees learn by doing.

Managers often use on-the-job training on a continuing basis to ensure that their subordinates keep up to date with changes in goals, technology, products, or customer needs and desires. For example, sales representatives at Mary Kay Cosmetics Inc. receive ongoing training so that they are not only knowledgeable about new cosmetic products and currently popular colors but also reminded of Mary Kay's guiding principles. Mary Kay's expansion into Russia has been very successful, in part because of the ongoing training that Mary Kay's Russian salespeople receive.⁵¹

Types of development

Although both classroom instruction and on-the-job training can be used for development purposes as well as training, development often includes additional activities such as varied work experiences and formal education.

VARIED WORK EXPERIENCES Top managers need to develop an understanding of, and expertise in, a variety of functions, products and services, and markets. To develop executives who will have this expertise, managers frequently make sure that employees with high potential have a wide variety of different job experiences, some in line positions and some in staff positions. Varied work experiences broaden employees' horizons and help them think more about the big picture. For example, one- to three-year stints overseas are being used increasingly to provide managers with international work experiences. With organizations becoming more global, managers need to develop an understanding of the different values, beliefs, cultures, regions, and ways of doing business in different countries.

Having a mentor (a *mentor* is an experienced member of an organization who provides advice and guidance to a less experienced member, called a *protégé*) can help managers seek out work experiences and assignments that will contribute to their development and gain the most they can from varied work experiences.⁵² While some mentors and protégés hook up informally, organizations have found that formal mentorship programs can be valuable ways to contribute to the development of managers and all employees, as indicated in the following "Focus on Diversity."



Focus on Diversity

Development Through Mentoring

Lynn Tyson, vice president for investor relations at Dell, never had a mentor help her navigate her rise to the top and says that "most of the time I was shaking in my shoes." Realizing the benefits of mentors for protégé development, and for the ability of organizations to retain valued members, Tyson worked to develop a formal mentoring program at Dell. Tyson currently mentors 40 protégés and derives tremendous satisfaction from knowing that she has "the ability to make a difference in somebody's career."⁵³

Formal mentoring programs ensure that mentoring takes place in an organization, structure the process, and make sure that diverse organizational members have equal access to mentors. Participants receive training, efforts are focused on matching up mentors and protégés so that meaningful developmental relationships ensue, and organizations can track reactions and assess the potential benefits of mentoring. Formal mentoring programs can also ensure that diverse members of an organization receive the benefits of mentoring. A recent study conducted by David A. Thomas, a professor at the Harvard Business School, found that members of racial minority groups at three large corporations who were very successful in their careers had the benefit of mentors. Clearly, all members of an organization can benefit from mentors; formal mentorship programs help organizations make this valuable development tool available to all employees.⁵⁴

When diverse members of an organization lack mentors, their progress in the organization and advancement to high-level positions can be hampered. Ida Abbott, a lawyer and consultant on work-related issues, recently presented a paper to the Minority Corporate Counsel Association in which she concluded, "The lack of adequate mentoring has held women and minority lawyers back from achieving professional success and has led to high rates of career dissatisfaction and attrition."⁵⁵

Mentoring can benefit all kinds of employees in all kinds of work.⁵⁶ John Washko, a manager at the Four Seasons hotel chain, benefited from the mentoring he received from Stan Bromley on interpersonal relations and how to deal with employees; mentor Bromley, in turn, found that participating in the Four Seasons mentoring program helped him develop his own management style.⁵⁷ More generally, development is an ongoing process for all managers, and mentors often find that mentoring contributes to their own personal development.

FORMAL EDUCATION Many large corporations reimburse employees for tuition expenses they incur while taking college courses and obtaining advanced degrees. This is not just benevolence on the part of the employer or even a simple reward given to the employee; it is an effective way to develop employees who are able to take on new responsibilities and more challenging positions. For similar reasons, corporations spend thousands of dollars sending managers to executive development programs such as executive MBA programs. In these programs, experts teach managers the latest in business and management techniques and practices.

To save time and travel costs, managers are increasingly relying on *long-distance learning* to formally educate and develop employees. Using videoconferencing technologies, business schools such as the Harvard Business School, the University of Michigan, and Babson College are teaching courses on video screens in corporate conference rooms. Business schools are also customizing courses and degrees to fit the development needs of employees in a particular company.

Transfer of training and development

Whenever training and development take place off the job or in a classroom setting, it is vital for managers to promote the transfer of the knowledge and skills acquired *to the actual work situation*. Trainees should be encouraged and expected to use their newfound expertise on the job.

Performance Appraisal and Feedback

performance appraisal

The evaluation of employees' job performance and contributions to their organization.

performance feedback

The process through which managers share performance appraisal information with subordinates, give subordinates an opportunity to reflect on their own performance, and develop, with subordinates, plans for the future.

The recruitment/selection and training/development components of a human resource management system ensure that employees have the knowledge and skills needed to be effective now and in the future. Performance appraisal and feedback complement recruitment, selection, training, and development. **Performance appraisal** is the evaluation of employees' job performance and contributions to the organization. **Performance feedback** is the process through which managers share performance appraisal information with their subordinates, give subordinates an opportunity to reflect on their own performance, and develop, with subordinates, plans for the future. Before performance feedback, performance appraisal must take place. Performance appraisal could take place without providing performance feedback, but wise managers are careful to provide feedback because it can contribute to employee motivation and performance.

Performance appraisal and feedback contribute to the effective management of human resources in several ways. Performance appraisal gives managers important information on which to base human resource decisions.⁵⁸ Decisions about pay raises, bonuses, promotions, and job moves all hinge on the accurate appraisal of performance. Performance appraisal can also help managers determine which workers are candidates for training and development and in what areas. Performance feedback encourages high levels of employee motivation and performance. It lets good performers know that their efforts are valued and appreciated. It also lets poor performers know that their lackluster performance needs improvement. Performance feedback can provide both good and poor performers with insight on their strengths and weaknesses and ways in which they can improve their performance in the future.

Types of performance appraisal

Performance appraisal focuses on the evaluation of traits, behaviors, and results.⁵⁹

TRAIT APPRAISALS When trait appraisals are used, managers assess subordinates on personal characteristics that are relevant to job performance, such as skills, abilities, or personality. A factory worker, for example, may be evaluated based on her ability to use computerized equipment and perform numerical calculations. A social worker may be appraised based on his empathy and communication skills.

Three disadvantages of trait appraisals often lead managers to rely on other appraisal methods. First, possessing a certain personal characteristic does not ensure that the personal characteristic will actually be used on the job and result in high performance. For example, a factory worker may possess superior computer and numerical skills but be a poor performer due to low motivation. The second disadvantage of trait appraisals is linked to the first. Because traits do not always show a direct association with performance, workers and courts of law may view them as unfair and potentially discriminatory. The third disadvantage of trait appraisals is that they often do not enable managers to provide employees with feedback that they can use to improve performance. Because trait appraisals focus on relatively enduring human characteristics that change only over the long term, employees

can do little to change their behavior in response to performance feedback from a trait appraisal. Telling a social worker that he lacks empathy provides him with little guidance about how to improve his interactions with clients, for example. These disadvantages suggest that managers should use trait appraisals only when they can demonstrate that the assessed traits are accurate and important indicators of job performance.

BEHAVIOR APPRAISALS Through behavior appraisals, managers assess how workers perform their jobs—the actual actions and behaviors that workers exhibit on the job. Whereas trait appraisals assess what workers are *like*, behavior appraisals assess what workers *do*. For example, with a behavior appraisal, a manager might evaluate a social worker on the extent to which he looks clients in the eye when talking with them, expresses sympathy when they are upset, and refers them to community counseling and support groups geared toward the specific problem they are encountering. Behavior appraisals are especially useful when *how* workers perform their jobs is important. In educational organizations such as high schools, for example, the number of classes and students taught is important, but also important is how they are taught or the methods teachers use to ensure that learning takes place.

Behavior appraisals have the advantage of providing employees with clear information about what they are doing right and wrong and how they can improve their performance. And because behaviors are much easier for employees to change than traits, performance feedback from behavior appraisals is more likely to lead to performance improvements.

RESULT APPRAISALS For some jobs, *how* people perform the job is not as important as *what* they accomplish or the results they obtain. With result appraisals, managers appraise performance by the results or the actual outcomes of work behaviors, as is the case at Semco in the “Management Snapshot.” Take the case of two new-car salespersons. One salesperson strives to develop personal relationships with her customers. She spends hours talking to them and frequently calls them up to see how their decision-making process is going. The other salesperson has a much more hands-off approach. He is very knowledgeable, answers customers’ questions, and then waits for them to come to him. Both salespersons sell, on average, the same number of cars, and the customers of both are satisfied with the service they receive, according to postcards that the dealership mails to customers asking for an assessment of their satisfaction. The manager of the dealership appropriately uses result appraisals (sales and customer satisfaction) to evaluate the salespeople’s performance because it does not matter which behavior salespeople use to sell cars as long as they sell the desired number and satisfy customers. If one salesperson sells too few cars, however, the manager can give that person performance feedback about his or her low sales.

OBJECTIVE AND SUBJECTIVE APPRAISALS Whether managers appraise performance in terms of traits, behaviors, or results, the information they assess is either objective or subjective. **Objective appraisals** are based on facts and are likely to be numerical—the number of cars sold, the number of meals prepared, the number of times late, the number of audits completed. Managers often use objective appraisals when results are being appraised because results tend to be easier to quantify than traits or behaviors. When *how* workers perform their jobs is

objective appraisal

An appraisal that is based on facts and is likely to be numerical.

subjective appraisal An appraisal that is based on perceptions of traits, behaviors, or results.

important, however, subjective behavior appraisals are more appropriate than result appraisals.

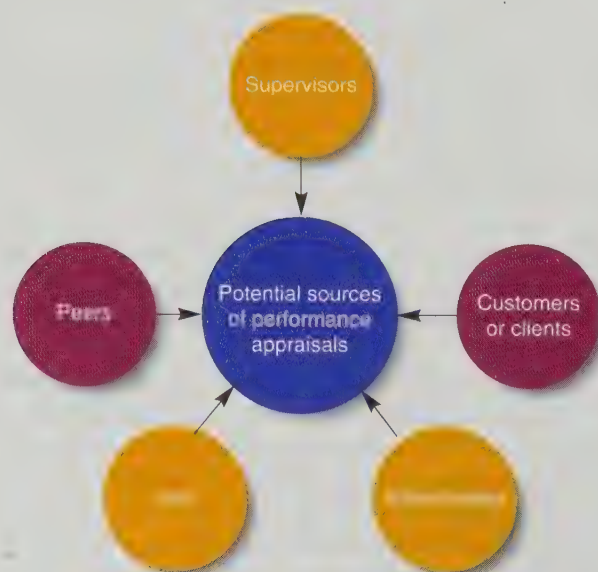
Subjective appraisals are based on managers' perceptions of traits, behaviors, or results. Because subjective appraisals rest on managers' perceptions, there is always the chance that they are inaccurate. This is why both researchers and managers have spent considerable time and effort on determining the best way to develop reliable and valid subjective measures of performance.

Who appraises performance?

We have been assuming that managers or the supervisors of employees evaluate performance. This is a pretty fair assumption, for supervisors are the most common appraisers of performance; indeed, each year 70 million U.S. citizens have their job performance appraised by their managers or supervisors.⁶⁰ Performance appraisal is an important part of most managers' job duties. Managers are responsible for not only motivating their subordinates to perform at a high level but also making many decisions hinging on performance appraisals, such as pay raises or promotions. Appraisals by managers can be usefully augmented by appraisals from other sources (see Figure 12.5).

SELF, PEERS, SUBORDINATES, AND CLIENTS When self-appraisals are used, managers supplement their evaluations with an employee's assessment of his or her own performance. Peer appraisals are provided by an employee's co-workers. Especially when subordinates work in groups or teams, feedback from peer appraisals can motivate team members while providing managers with important information for decision making. A growing number of companies are having subordinates appraise their managers' performance and leadership as well. And sometimes customers or clients provide assessments of employee performance in terms of responsiveness to customers and quality of service. Although appraisals

Figure 12.5
Who Appraises Performance?



from each of these sources can be useful, managers need to be aware of potential issues that may arise when they are used. Subordinates sometimes may be inclined to inflate self-appraisals, especially if organizations are downsizing and they are worried about their job security. Managers who are appraised by their subordinates may fail to take needed but unpopular actions out of fear that their subordinates will appraise them negatively.

360-degree appraisal

A performance appraisal by peers, subordinates, superiors, and sometimes clients who are in a position to evaluate a manager's performance.

360-DEGREE PERFORMANCE APPRAISALS To improve motivation and performance, some organizations include 360-degree appraisals and feedback in their performance appraisal systems, especially for managers. In a **360-degree appraisal**, a variety of people, beginning with the manager and including peers or co-workers, subordinates, superiors, and sometimes even customers or clients, appraise a manager's performance. The manager receives feedback based on evaluations from these multiple sources.

The growing number of companies using 360-degree appraisals and feedback include AT&T Corp., Allied Signal Inc., Eastman Chemical Co., and Baxter International Inc.⁶¹ For 360-degree appraisals and feedback to be effective, there has to be trust throughout an organization. More generally, trust is a critical ingredient in any performance appraisal and feedback procedure. In addition, research suggests that 360-degree appraisals should focus on behaviors rather than traits or results and that managers need to carefully select appropriate raters. Moreover, appraisals tend to be more honest when made anonymously, as is the case at Semco in the "Management Snapshot," and when raters have been trained in how to use 360-degree appraisal forms.⁶² Additionally, managers need to think carefully about the extent to which 360-degree appraisals are appropriate for certain jobs and be willing to modify any system they implement when they become aware of unintended problems the appraisal system is responsible for.⁶³

Even when 360-degree appraisals are used, it is sometimes difficult to design an effective process by which subordinates' feedback can be communicated to their managers. Advances in information technology provide organizations with a potential solution to this problem. For example, ImproveNow.com has online questionnaires that subordinates can fill out to evaluate the performance of their managers and provide the managers with feedback. Each subordinate of a particular manager completes the questionnaire independently, all responses are tabulated, and the manager is given specific feedback on behaviors in a variety of areas, such as rewarding good performance, looking out for subordinates' best interest and being supportive, and having a vision for the future.⁶⁴

For example, Sonia Russomanno, a manager at Alliance Funding, a New Jersey mortgage lending organization, received feedback from her nine subordinates online from ImproveNow. She received an overall grade of B and specific feedback on a variety of dimensions. This experience drove home to Russomanno the importance of getting honest feedback from her subordinates and listening to it to improve her performance as a manager. She has changed how she rewards her subordinates as a result and plans on using this service in the future to see how she is doing.⁶⁵

Effective performance feedback

For the performance appraisal and feedback component of a human resource management system to encourage and motivate high performance, managers must

formal appraisal

An appraisal conducted at a set time during the year and based on performance dimensions and measures that were specified in advance.

provide their subordinates with performance feedback. To generate useful information to feed back to their subordinates, managers can use both formal and informal appraisals. **Formal appraisals** are conducted at set times during the year and are based on performance dimensions and measures that have been specified in advance.

Managers in most large organizations use formal performance appraisals on a fixed schedule dictated by company policy, such as every six months or every year. An integral part of a formal appraisal is a meeting between the manager and the subordinate in which the subordinate is given feedback on performance. Performance feedback lets subordinates know which areas they are excelling in and which areas need improvement; it also should provide them with guidance for improving performance.

Realizing the value of formal appraisals, managers in many large corporations have committed substantial resources to updating their performance appraisal procedures and training low-level managers in how to use them and provide accurate feedback to employees. Top managers at the pharmaceutical company Hoffmann-La Roche Inc., for example, recently spent \$1.5 million updating and improving their performance appraisal procedures. Alan Rubino, vice president of human resources for Hoffmann-La Roche, believes that this was money well spent because “people need to know exactly where they stand and what’s required of them.” Before Hoffmann-La Roche’s new system was implemented, managers attended a three-day training and development session to improve their performance appraisal skills. The new procedures call for every manager and subordinate to develop a performance plan for subordinates for the coming year—a plan that is linked to the company’s strategy and goals and approved by the manager’s own superiors. Formal performance appraisals are conducted every six months, during which actual performance is compared to planned performance.⁶⁶

Formal performance appraisals supply both managers and subordinates with valuable information; but subordinates often want feedback on a more frequent basis, and managers often want to motivate subordinates as the need arises. For these reasons many companies, including Hoffman-La Roche, supplement formal performance appraisal with frequent **informal appraisals**, for which managers and their subordinates meet as the need arises to discuss ongoing progress and areas for improvement. Moreover, when job duties, assignments, or goals change, informal appraisals can provide workers with timely feedback concerning how they are handling their new responsibilities.

Managers often dislike providing performance feedback, especially when the feedback is negative, but doing so is an important managerial activity.⁶⁷ Here are some guidelines for giving effective performance feedback that contributes to employee motivation and performance:

- ✱ *Be specific and focus on behaviors or outcomes that are correctable and within a worker’s ability to improve.* Example: Telling a salesperson that he is too shy when interacting with customers is likely to do nothing more than lower his self-confidence and prompt the salesperson to become defensive. A more effective approach would be to give the salesperson feedback about specific behaviors to engage in—greeting customers as soon as they enter the department, asking customers whether they need help, and volunteering to help customers find items if they seem to be having trouble.

informal appraisal

An unscheduled appraisal of ongoing progress and areas for improvement.

- *Approach performance appraisal as an exercise in problem solving and solution finding, not criticizing.* Example: Rather than criticizing a financial analyst for turning in reports late, the manager helps the analyst determine why the reports are late and identify ways to better manage her time.
- *Express confidence in a subordinate's ability to improve.* Example: Instead of being skeptical, a first-level manager tells a subordinate that he is confident that the subordinate can increase quality levels.
- *Provide performance feedback both formally and informally.* Example: The staff of a preschool receives feedback from formal performance appraisals twice a year. The director of the school also provides frequent informal feedback such as complimenting staff members on creative ideas for special projects, noticing when they do a particularly good job handling a difficult child, and pointing out when they provide inadequate supervision.
- *Praise instances of high performance and areas of a job in which a worker excels.* Example: Rather than focusing on just the negative, a manager discusses the areas her subordinate excels in as well as the areas in need of improvement.
- *Avoid personal criticisms and treat subordinates with respect.* Example: An engineering manager acknowledges her subordinates' expertise and treats them as professionals. Even when the manager points out performance problems to subordinates, she refrains from criticizing them personally.
- *Agree to a timetable for performance improvements.* Example: A first-level manager and his subordinate decide to meet again in one month to determine if quality levels have improved.

In following these guidelines, managers need to remember why they are giving performance feedback: to encourage high levels of motivation and performance. Moreover, the information that managers gather through performance appraisal and feedback helps them determine how to distribute pay raises and bonuses.

Pay and Benefits

Pay includes employees' base salaries, pay raises, and bonuses and is determined by a number of factors such as characteristics of the organization and the job and levels of performance. Employee *benefits* are based on membership in an organization (and not necessarily on the particular job held) and include sick days, vacation days, and medical and life insurance. In Chapter 9, we discussed the ways in which pay can motivate organizational members to perform at a high level, as well as the different kinds of pay plans managers can use to help an organization achieve its goals and gain a competitive advantage. As you will learn, it is important for pay to be linked to behaviors or results that contribute to organizational effectiveness. Next, we focus on establishing an organization's pay level and pay structure.

pay level The relative position of an organization's pay incentives in comparison with those of other organizations in the same industry employing similar kinds of workers.

Pay level

Pay level is a broad comparative concept that refers to how an organization's pay incentives compare, in general, to those of other organizations in the same industry employing similar kinds of workers. Managers must decide if they want to



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offer relatively high wages, average wages, or relatively low wages. High wages help ensure that an organization is going to be able to recruit, select, and retain high performers, but high wages also raise costs. Low wages give an organization a cost advantage but may undermine the organization's ability to select and recruit high performers and to motivate current employees to perform at a high level. Either of these situations may lead to inferior quality or inadequate customer service.

In determining pay levels, managers should take into account their organization's strategy. A high pay level may prohibit managers from effectively pursuing a low-cost strategy. But a high pay level may be well worth the added costs in an organization whose competitive advantage lies in superior quality and excellent customer service. As one might expect, hotel and motel chains with a low-cost strategy, such as Days Inn and Hampton Inns, have lower pay levels than chains striving to provide high-quality rooms and services, such as Four Seasons and Hyatt Regency.

Pay structure


pay structure The arrangement of jobs into categories reflecting their relative importance to the organization and its goals, level of skill required, and other characteristics.

After deciding on a pay level, managers have to establish a pay structure for the different jobs in the organization. A **pay structure** clusters jobs into categories reflecting their relative importance to the organization and its goals, levels of skill required, and other characteristics managers consider to be important. Pay ranges are established for each job category. Individual jobholders' pay within job categories is then determined by factors such as performance, seniority, and skill levels.

There are some interesting global differences in pay structures. Large corporations based in the United States tend to pay their CEOs and top managers higher salaries than do their European or Japanese counterparts. There also is a much greater pay differential between employees at the bottom of the corporate hierarchy and those higher up the hierarchy in U.S. companies than in European or Japanese companies.⁶⁸

Concerns have been raised over whether it is equitable or fair for CEOs of large companies in the United States to be making hundreds of thousands or millions of dollars in years when their companies are restructuring and laying off a large portion of their workforces.⁶⁹ Robert Allen, for example, the CEO of AT&T, came under intense scrutiny in 1996 because he was earning \$5 million a year when AT&T announced plans to lay off thousands of employees. As

indicated in the following “Ethics in Action,” hefty pay packages for current top managers, and those leaving top-management posts, are alive and well in corporate America.



Ethics in Action

Is CEO Pay over the Top?

CEOs in the United States continue to earn phenomenal amounts of money despite public outcry and disgruntled shareholders. According to *BusinessWeek* magazine, for the three-year period from 2001 to 2003, the 25 highest-paid U.S. CEOs earned an average of \$32.7 million a year, which is over 900 times larger than the salary of the typical U.S. worker.⁷⁰ In 2004, the average total CEO pay was \$9.6 million, 15 percent higher than the average CEO pay of \$8.3 million in 2003. Average pay levels for rank and file employees increased by 2.9 percent from 2003 to 2004; in 2004, the average worker earned \$33,176.⁷¹ Is a pay structure with such a huge pay differential between those at the very top and average employees ethical? Shareholders and the public are increasingly asking this very question and are asking large corporations to rethink their pay structures.⁷² As a result of increasing scrutiny, pay levels of top managers are much more likely to be linked to the performance of their companies and their meeting of predetermined targets than they were before.⁷³

Even more mind-boggling are the severance packages some CEOs and top managers receive when they leave their organizations. Steven Heyer was president and chief operating officer for Coca-Cola for three years; upon departing the company in June 2004, he received a \$24 million severance package.⁷⁴ Departing Coca-Cola CEO Douglas Daft received over \$30 million in a severance package in 2004 even though the company's performance was far less than stellar during his leadership. Douglas Ivestor, CEO of Coca-Cola prior to Daft, continues to receive \$675,000 per year from a consulting contract with the company, even though he received over \$100 million in his severance package.⁷⁵

Coca-Cola is not alone in paying phenomenal severance pay to departing top managers. For example, when Richard H. Brown left Electronic Data Systems Corp. as CEO in 2003 amid poor financial performance, he received a severance package of over \$45 million. Leo Mullins, who retired from his position as CEO of Delta Airlines, received over \$15 million in severance compensation.⁷⁶ Carly Fiorina received a \$21 million severance package when she stepped down from her position as CEO of Hewlett-Packard in 2005.⁷⁷

Why do companies pay departing executives so excessively? Some say offering such “golden parachutes” is necessary to recruit top talent. For some companies, generous departing payouts help ensure that confidential company information stays confidential and that ex-CEOs do not damage the reputations of the company with negative statements to the press.⁷⁸ In any case, in an era in which many workers are struggling to find and keep jobs and make ends meet, more and more people are questioning whether it is ethical for some top managers to be making so much money. Granted, some very highly paid CEOs have done wonders for their companies and created real value.⁷⁹ But what about those poorly performing CEOs who are pushed from their jobs with millions in severance pay to break their fall?

Benefits

Organizations are legally required to provide certain benefits to their employees, including workers' compensation, Social Security, and unemployment insurance. Workers' compensation provides employees with financial assistance if they become unable to work due to a work-related injury or illness. Social Security provides financial assistance to retirees and disabled former employees. Unemployment insurance provides financial assistance to workers who lose their jobs due to no fault of their own. The legal system in the United States views these three benefits as ethical requirements for organizations and thus mandates that they be provided.

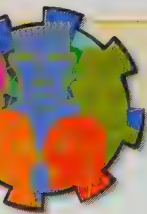
Other benefits such as health insurance, dental insurance, vacation time, pension plans, life insurance, flexible working hours, company-provided day care, and employee assistance and wellness programs are provided at the option of employers. Benefits enabling workers to simultaneously balance the demands of their jobs and of their lives away from the office or factory are of growing importance for many workers who have competing demands on their all-too-scarce time and energy.

In some organizations, top managers determine which benefits might best suit the employees and organization and offer the same benefit package to all employees. Other organizations, realizing that employees' needs and desires might differ, offer **cafeteria-style benefit plans** that let employees themselves choose the benefits they want. Cafeteria-style benefit plans sometimes assist managers in dealing with employees who feel unfairly treated because they are unable to take advantage of certain benefits available to other employees who, for example, have children. Some organizations have success with cafeteria-style benefit plans; others find them difficult to manage.

More and more managers are viewing benefits as a means of attracting and retaining valued employees and helping these employees stay healthy, as indicated in the following "Focus on Diversity."

cafeteria benefit

plan A plan from which employees can choose the benefits that they want.

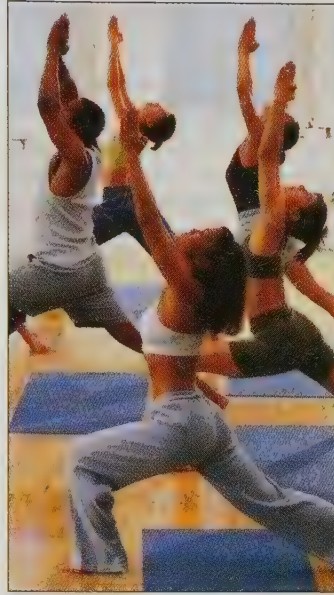


Focus on Diversity

Keeping Employees Happy and Healthy with Benefits

As health care costs are escalating and overstretched employees are finding it hard to take time out to exercise and take care of their health, more companies are providing benefits and incentives to promote employee wellness. Astra Zeneca International offers its employees on-site counseling with a nutritionist and pays employees \$125 for voluntarily taking a health risk assessment that covers wellness-related factors such as weight and nutrition.⁸⁰ Dole Food Company rewards employees with points toward gift certificates for participating in wellness activities provided on-site, such as yoga classes.⁸¹

For new working parents, leaving an infant with a caregiver for 8 or 10 hours a day can be traumatic. To ease the trauma and allow new parents to bond with their babies, Health Newsletter Direct, based in Evanston, Illinois, allows employees to bring their babies to work.⁸² Since the program was first instituted,



More and more companies are promoting employee wellness by providing incentives such as points toward gift certificates for participating in yoga classes.

14 parents have taken advantage of it. Mark Tatara, the first father to bring his baby to work, says this of the program: "The closeness with my child means more to me than I ever could have imagined . . . and my co-workers were excited about him being here."⁸³

Same-sex domestic-partner benefits are also being used to attract and retain valued employees. Gay and lesbian workers are more and more reluctant to work for companies that do not provide them with the same kinds of benefits for their partners as those provided for partners of the opposite sex.⁸⁴ Kevin Ryan, CEO of DoubleClick, a budding high-tech company in New York that hired 80 new employees in the first two and a half months of 2004 due to its rapid growth trajectory, indicates that it is a business necessity for his workplace to welcome gay and lesbian employees.⁸⁵ His key concern is hiring the best, highly skilled people; once hired, all employees are welcome and afforded the same benefits regardless of their sexual orientation.⁸⁶

Labor Relations

labor relations

The activities that managers engage in to ensure that they have effective working relationships with the labor unions that represent their employees' interests.

Labor relations are the activities that managers engage in to ensure that they have effective working relationships with the labor unions that represent their employees' interests. Although the U.S. government has responded to the potential for unethical organizations and unfair treatment of workers by creating and enforcing laws regulating employment (including the EEO laws listed in Table 12.1), some workers believe that a union will ensure that their interests are fairly represented in their organizations.

Before we describe unions in more detail, let's take a look at some examples of important employment legislation. In 1938 the government passed the Fair Labor Standards Act, which prohibited child labor and made provisions for minimum wages, overtime pay, and maximum working hours to protect workers' rights. In 1963 the Equal Pay Act mandated that men and women performing equal work (work requiring the same levels of skill, responsibility, and effort performed in the same kind of working conditions) receive equal pay (see Table 12.1). In 1970 the Occupational Safety and Health Act mandated procedures for managers to follow to ensure workplace safety. These are just a few of the U.S. government's efforts to protect workers' rights. State legislatures also have been active in promoting safe, ethical, and fair workplaces.

Unions

Unions exist to represent workers' interests in organizations. Given that managers have more power than rank-and-file workers and that organizations have multiple stakeholders, there is always the potential that managers might take steps that

benefit one set of stakeholders such as shareholders while hurting another such as employees. For example, managers may decide to speed up a production line to lower costs and increase production in the hopes of increasing returns to shareholders. Speeding up the line, however, could hurt employees forced to work at a rapid pace and may increase the risk of injuries. Also, employees receive no additional pay for the extra work they are performing. Unions would represent workers' interests in a scenario such as this one.

Congress acknowledged the role that unions could play in ensuring safe and fair workplaces when it passed the National Labor Relations Act of 1935. This act made it legal for workers to organize into unions to protect their rights and interests and declared certain unfair or unethical organizational practices to be illegal. The National Labor Relations Act also established the National Labor Relations Board (NLRB) to oversee union activity. Currently, the NLRB conducts certification elections, which are held among the employees of an organization to determine whether they want a union to represent their interests. The NLRB also makes judgments concerning unfair labor practices and specifies practices that managers must refrain from.

Employees might vote to have a union represent them for any number of specific reasons.⁸⁷ They may think that their wages and working conditions are in need of improvement. They may believe that managers are not treating them with respect. They may think that their working hours are unfair or that they need more job security or a safer work environment. Or they may be dissatisfied with management and find it difficult to communicate their concerns to their bosses. Regardless of the specific reason, one overriding reason is power: A united group inevitably wields more power than an individual, and this type of power may be especially helpful to employees in some organizations.

Although these would seem to be potent forces for unionization, some workers are reluctant to join unions. Sometimes this reluctance is due to the perception that union leaders are corrupt. Some workers may simply believe that belonging to a union might not do them much good or may actually cause more harm than good while costing them money in membership dues. Employees also might not want to be forced into doing something they do not want to, such as striking because the union thinks it is in their best interest. Moreover, although unions can be a positive force in organizations, sometimes they also can be a negative force, impairing organizational effectiveness. For example, when union leaders resist needed changes in an organization or are corrupt, organizational performance can suffer.

The percentage of U.S. workers represented by unions today is smaller than it was in the 1950s, an era when unions were especially strong.⁸⁸ The American Federation of Labor–Congress of Industrial Organizations (AFL-CIO) includes 64 voluntary member unions representing 13 million workers.⁸⁹ Union influence in manufacturing and heavy industries has been on the decline, presumably because their workers no longer see the need to be represented by unions. Recently unions have made inroads in other segments of the workforce, however, particularly the low-wage end. Garbage collectors in New Jersey, poultry plant workers in North Carolina, and janitors in Baltimore are among the growing numbers of low-paid workers who are currently finding union membership attractive. North Carolina poultry workers voted in a union in part because they thought it was unfair that they had to buy their own gloves and hairnets used on the job and had to ask their supervisors' permission to go to the restroom.⁹⁰ Union membership and leadership, traditionally dominated by white men, is also becoming increasingly diverse.

collective bargaining

Negotiations between labor unions and managers to resolve conflicts and disputes about issues such as working hours, wages, benefits, working conditions, and job security.

Collective bargaining

Collective bargaining is negotiation between labor unions and managers to resolve conflicts and disputes and important issues such as working hours, wages, working conditions, and job security. Before sitting down with management to negotiate, union members sometimes go on strike to drive home their concerns to managers. Once an agreement that union members support has been reached (sometimes with the help of a neutral third party called a *mediator*), union leaders and managers sign a contract spelling out the terms of the collective bargaining agreement.

Union members sometimes go on strike when managers make decisions that the members think will hurt them and are not in their best interests. This is precisely what happened in 1996 when General Motors' North American assembly plants employing 177,000 workers were idled for 18 days. The strike originated in GM's Dayton, Ohio, brake assembly plants due to management's decision to buy some parts from other companies rather than make them in GM's own plants.⁹¹ The United Auto Workers Union called a strike because outsourcing threatens union members' jobs. The agreement that the union and management, bargaining collectively, reached allowed the outsourcing to continue but contained provisions for the creation of hundreds of new jobs as well as for improvements in working conditions.⁹²

Summary and Review

STRATEGIC HUMAN RESOURCE MANAGEMENT

Human resource management (HRM) includes all the activities that managers engage in to ensure that their organizations are able to attract, retain, and effectively utilize human resources.

Strategic HRM is the process by which managers design the components of a human resource management system to be consistent with each other, with other elements of organizational architecture, and with the organization's strategies and goals.

RECRUITMENT AND SELECTION

Before recruiting and selecting employees, managers must engage in human resource planning and job analysis. Human resource planning includes all the activities managers engage in to forecast their current and future needs for human resources. Job analysis is the process of identifying (1) the tasks, duties, and responsibilities that make up a job and (2) the knowledge, skills, and abilities needed to perform the job. Recruitment includes all the activities that managers engage in to develop a pool of qualified applicants for open positions. Selection is the process by which managers determine the relative qualifications of job applicants and their potential for performing well in a particular job.

TRAINING AND DEVELOPMENT

Training focuses on teaching organizational members how to perform effectively in their current jobs. Development focuses on broadening organizational members' knowledge and skills so that they will be prepared to take on new responsibilities and challenges.

PERFORMANCE APPRAISAL AND FEEDBACK

Performance appraisal is the evaluation of employees' job performance and contributions to the

organization. Performance feedback is the process through which managers share performance appraisal information with their subordinates, give them an opportunity to reflect on their own performance, and develop with them plans for the future. Performance appraisal provides managers with useful information for decision-making purposes. Performance feedback can encourage high levels of motivation and performance.

PAY AND BENEFITS Pay level is the relative position of an organization's pay incentives in comparison with those of other organizations in the same industry employing similar workers. A pay structure clusters jobs into categories according to their relative importance to the organization and its goals, the levels of skills required, and other characteristics. Pay ranges are then established for each job category. Organizations are legally required to provide certain benefits to their employees; other benefits are provided at the discretion of employers.

LABOR RELATIONS Labor relations include all the activities managers engage in to ensure that they have effective working relationships with the labor unions that may represent their employees' interests. The National Labor Relations Board oversees union activity. Collective bargaining is the process through which labor unions and managers resolve conflicts and disputes and negotiate agreements.



Management in Action

Topics for Discussion and Action

Discussion

1. Discuss why it is important for human resource management systems to be in sync with an organization's strategy and goals and with each other.
2. Discuss why training and development are ongoing activities for all organizations.
3. Describe the type of development activities you think middle managers are most in need of.
4. Evaluate the pros and cons of 360-degree performance appraisals and feedback. Would you like your performance to be appraised in this manner? Why or why not?
5. Discuss why two restaurants in the same community might have different pay levels.
6. Explain why union membership is becoming more diverse.

Action

7. Interview a manager in a local organization to determine how that organization recruits and selects employees.



Building Management Skills

Analyzing Human Resource Systems

Think about your current job or a job that you have had in the past. If you have never had a job, then interview a friend or family member who is currently working. Answer the following questions about the job you have chosen:

1. How are people recruited and selected for this job? Are the recruitment and selection procedures that the organization uses effective or ineffective? Why?
2. What training and development do people who hold this job receive? Is it appropriate? Why or why not?
3. How is performance of this job appraised? Does performance feedback contribute to motivation and high performance on this job?
4. What levels of pay and benefits are provided on this job? Are these levels of pay and benefits appropriate? Why or why not?



Small Group Breakout Exercise

Building a Human Resource Management System

Form groups of three or four people, and appoint one group member as the spokesperson who will communicate your findings to the whole class when called upon by the instructor. Then discuss the following scenario.

You and your two or three partners are engineers who minored in business at college and have decided to start a consulting

business. Your goal is to provide manufacturing-process engineering and other engineering services to large and small organizations. You

forecast that there will be an increased use of outsourcing for these activities. You discussed with managers in several large organizations



the services you plan to offer, and they expressed considerable interest. You have secured funding to start your business and now are building the HRM system. Your human resource planning suggests that you need to hire between five and eight experienced engineers with good communication skills, two clerical/secretarial workers, and two MBAs who between them have financial, accounting, and human

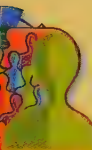
resource skills. You are striving to develop your human resources in a way that will enable your new business to prosper.

1. Describe the steps you will take to recruit and select (a) the engineers, (b) the clerical/secretarial workers, and (c) the MBAs.
2. Describe the training and development the engineers, the clerical/secretarial

workers, and the MBAs will receive.

3. Describe how you will appraise the performance of each group of employees and how you will provide feedback.
4. Describe the pay level and pay structure of your consulting firm.

Be the Manager



You are Walter Michaels and have just received some disturbing feedback. You are the director of human resources for Maxi Vision Inc., a medium-size window and glass-door manufacturer. You recently initiated a 360-degree performance appraisal system for all middle and upper managers at Maxi Vision, including yourself but excluding the most senior executives and the top-management team.

You were eagerly awaiting the feedback you would receive from the managers who report to you; you had recently implemented several important initiatives that affected them and their subordinates, including a complete overhaul of the organization's performance appraisal system. While the managers who report to you were evaluated based on 360-degree appraisals,

their own subordinates were evaluated using a 20-question BARS scale you recently created that focuses on behaviors. Conducted annually, appraisals are an important input into pay raise and bonus decisions.

You were so convinced that the new performance appraisal procedures were highly effective that you hoped your own subordinates would mention them in their feedback to you. And boy did they! You were amazed to learn that the managers and their subordinates thought the new BARS scales were unfair, inappropriate, and a waste of time. In fact, the managers' feedback to you was that their own performance was suffering, based on the 360-degree appraisals they received, because their subordinates hated the new appraisal system

and partially blamed their bosses, who were part of management. Some managers even admitted giving all their subordinates approximately the same scores on the scales so that their pay raises and bonuses would not be affected by their performance appraisals.

You couldn't believe your eyes when you read these comments. You had spent so much time developing what you thought was the ideal rating scale for this group of employees. Evidently, for some unknown reason, they were being very closed-minded and wouldn't give it a chance. Your own supervisor was aware of these complaints and said that it was a top priority for you to fix "this mess" (with the implication that you were responsible for creating it). What are you going to do?



Additional Activities on the Build Your Management Skills DVD

- **Test Your Knowledge:**
 - (1) Stages of the Strategic HRM Process, (2) Training Methods, (3) Appraisal Methods, (4) Potential Errors in the Rating Process, (5) Recruitment Sources, and (6) Reliability and Validity
- **Self-Assessment:** What Is Your Communication Style Under Stress?
- **Manager's Hot Seat:** Diversity in Hiring: Candidate Conundrum

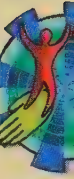
Managing Ethically

Some managers do not want to become overly friendly with their subordinates because they are afraid that if they do so, their objectivity when conducting performance appraisals and making decisions about pay raises and promotions will be impaired. Some subordinates resent it when they see one or more of their co-

workers being very friendly with the boss; they are concerned about the potential for favoritism. Their reasoning runs something like this: If two subordinates are equally qualified for a promotion and one is a good friend of the boss and the other is a mere acquaintance, who is more likely to receive the promotion?

Questions

1. Either individually or in a group, think about the ethical implications of managers' becoming friendly with their subordinates.
2. Do you think that managers should feel free to socialize and become good friends with their subordinates outside the workplace if they so desire? Why or why not?



BusinessWeek

Case in the News

It's a blustery thursday morning, and Liam E. McGee is a man on a mission as he marches briskly into a Fleet Bank branch in Boston's historic district. McGee isn't here to cash a check. Rather, as president of Bank of America Corp.'s consumer and small-business division, he's making spot checks on some of the 1,500 branches the bank inherited when it bought FleetBoston Financial Corp. last April. Striding through an eerily long corridor that winds back to the teller windows, the 50-year-old Irishman frowns as he navigates the quirky floor plan. "Layouts like this are just one of the challenges we have," he says. Finally inside the lobby, though, McGee is pleased to see the branch manager and reps engaging customers as they enter. "If you'd visited here six months ago, you would have seen all these people hidden back in their offices," he says.

So far, McGee's efforts to integrate FleetBoston's consumer businesses into Bank of America appear to be paying off—much to the surprise of Wall Street. The markets roundly panned the \$47 billion deal—one of the largest bank

mergers ever—when it was unveiled in October, 2003. The concern was that BofA had grossly overpaid for FleetBoston, which had been notorious among customers for poor service and on Wall Street for lackluster financial performance. The deal was initially marred by a heavy exodus of Fleet executives as well as a spate of negative headlines after Boston politicians accused BofA of breaking its initial pledge that there would be not net job losses in New England as a result of the merger.

But thanks in large part to McGee's sweeping makeover of Fleet's branch network, the deal is looking like a winner. After several years during which Fleet lost customers, Bank of America added 184,000 new consumer checking accounts and 196,000 savings accounts last year in Fleet's old stomping grounds. BofA achieved that growth while wringing \$909 million in costs from FleetBoston, slightly more than it had projected. The result: Fourth-quarter profits at the original Bank of America and the old FleetBoston grew 12 percent, to \$3.85 billion. Over the past

BofA's Happy Surprise

year, BofA's shares have risen 16.9 percent, versus a 6.3 percent return for the Philadelphia KBW Bank Index. The Fleet deal "has gone far better than I anticipated," says Steven Wharton, a portfolio manager at Morgan Stanley Financial Services Trust, who holds 440,200 BofA shares.

Rising Star

McGee's role has not gone unnoticed. If he can maintain the heady performance of the consumer unit, some BofA watchers believe that he will be one of the favorites to succeed Bank of America Chief Executive Kenneth D. Lewis. Lewis, 57, is fully expected to remain in charge until he's 65. But BofA watchers look for Lewis to anoint a successor by the end of the decade. "[McGee] is the rising star right now," says one former BofA executive.

Banking wasn't the first career choice for McGee, whose father worked as a Los Angeles bus driver after moving his family from Ireland when Liam was a child. McGee's initial brush with banking was a

brief job as a teller during college. "The truth is, I hated it—back then it was all about paperwork, audits, and initialing forms," he recalls. But after earning a law degree from Loyola Marymount University, McGee rejected a career in law for a job as a lending officer for a small California bank. After stints at Wells Fargo & Co. and Security Pacific Corp., he eventually rose to oversee technology and operations for the old San Francisco-based BankAmerica Corp.

After NationsBank Corp. in Charlotte, N.C., acquired BankAmerica—and adopted the Bank of America name—McGee's star really began to rise. While many execs from San Francisco bailed out, McGee bought into the deal. As head of BofA's Southern California operations, he was instrumental in rallying the old BofA's demoralized workforce through whirlwind branch visits and regionwide voicemails. And when the city councils of Santa Monica, Calif., and San Francisco enacted ordinances to prohibit BofA from levying ATM surcharges on non-customers, it was McGee who stepped in front of the TV cameras and helped turn public sentiment against the bans. The California courts ultimately ruled that they were unconstitutional: "More than any other individual, Liam turned it around for BofA in California," says one former BofA manager who worked closely with McGee at the time.

The key to BofA's unexpected success with FleetBoston, say analysts, has been the efforts of McGee and his team to overhaul Fleet's branches, from products to training to culture. To lure new customers, BofA dangled free checking and free online bill-paying, a service for which many New England banks still charged. And while the old FleetBoston simply gave customers the 800 number for an outside mort-

gage lender, BofA has outfitted roughly two-thirds, of Fleet branches with special software that approves or rejects a customer's application for a mortgage or home-equity loans within 30 minutes.

At the same time, Bank of America recruited dozens of new branch managers and reps from retailers with strong service cultures, such as Target Corp. It also adopted a few touches from Walt Disney Co. (Employees are now "on stage" when they're meeting with customers and "off stage" when they're in a back office handling paperwork.) And he implemented an exhaustive "playbook" that has scripts for everything down to the language with which tellers are supposed to greet customers. Still, at one Boston branch McGee visited, Paul J. Hillson, a consumer marketing manager, concedes that he encountered initial resistance from some FleetBoston tellers: "What you hear is 'But I already know that customer.'" McGee agrees that changing employee behavior "is still a work in progress."

Measuring each branch's performance and giving employees feedback are critical parts of the makeover. BofA brought in Six Sigma specialists to develop systems to generate reports on everything from customer satisfaction to sales productivity at each branch so that district managers can quickly intervene at underperforming offices. Already, each Fleet branch employee is signing up customers each day for an average of 4.1 new products, such as savings accounts and credit cards. That figure has more than doubled since the merger, from 1.9, and McGee expects it to hit 6.4 this year. To prevent branch employees from indiscriminately flogging new products, BofA redesigned its pay plan to rescind bonuses paid for sales of any

products that customers cancel within four months. "I don't want our associates just pounding product that customers really don't need," says McGee.

Software Switch

McGee isn't out of the woods yet with FleetBoston. The biggest test comes this summer, when BofA switches Fleet's branches over to its own software platform—a process that, more than anything else, can lead to the service glitches that trigger customer defections. And some rivals contend that any gains BofA is making on the retail side are being partially offset by the defections of Fleet's old commercial-lending offices to other banks.

McGee acknowledges some loss of lending officers, but he denies that it has resulted in "anything close to a material nature" in lost loan volume. If that's the strongest criticism competitors can level, McGee has more than the luck of the Irish going for him.

Questions

1. What changes did Liam McGee make to human resource practices and procedures at Fleet Boston once Bank of America acquired it?
2. Why did Bank of America recruit new branch managers for some Fleet branches?
3. Why is performance measurement and provision of feedback being emphasized in the branches?
4. How and why did Bank of America alter the pay plan at the branches?

Source: D. Foust and M. Eidam, "BofA's Happy Surprise." Reprinted from the February 7, 2005, issue of *BusinessWeek* by special permission. Copyright © 2005 by the McGraw-Hill Companies, Inc.

March 26 heralds the opening of the spring season in India, a day celebrated with riotous color and revelry. But in one corner of Bangalore, India's info tech hub, the sunny Saturday is heavy with tension. At an Internet cafe, a group of engineers and math majors, all in their 20s, hunch over terminals, ready to write some killer code—and, with luck, launch careers with one of the world's premier tech companies, Google Inc.

It's the Google India Code Jam, a contest to find the most brilliant coder in South and Southeast Asia. The fastest will win \$6,900—and more important, the offer of a coveted job at one of Google's research and development centers. At the stroke of 10:30 a.m., the contestants begin, emerging exhausted three hours later. "It's been incredibly difficult and awesome," says Nitin Gupta, a computer science undergrad at the Indian Institute of Technology at Bombay.

Google has staged Code Jams in the U.S., but this is its first such bakeoff in Asia, and the response is huge. Some 14,000 aspirants registered from all over South and Southeast Asia for the first round in February. The top 50 were selected for the finals in Bangalore: 39 from India, 8 from Singapore, and 3 from Indonesia. "It's a dog-eat-dog world," says Robert Hughes president of TopCoder Inc., the Glastonbury (Conn.) testing company that runs the Code Jams. "Wherever the best talent is, Google wants them."

And the winner is . . . one of these clever IIT grads from India, right? Surprisingly, no. Ardian Poernomo, a third-year undergrad

computer engineering student at Singapore's Nanyang Technological University, lands in first place. The No. 2 finisher, Pascal Alfadian, a second-year student at the Universitas Katolik Parahyangan in West Java, is Indonesian, too. Poernomo didn't commit to taking a job with Google, however: He may go for a PhD in computer science in the U.S.

Still, Google now has a new pool of Asian talent to choose from. According to Krishna Bharat, head of Google's India R&D center, all the finalists will be offered jobs. And Google needs them. The search company has been frustrated by its inability to find top-notch engineers for its year-old Indian center, according to industry insiders. Its Bangalore staff now totals 25, but it was hoping to have signed up at least 100 engineers by last December. Bharat refuses to discuss the company's difficulty in filling its ranks, except to say: "It has been a challenging year."

War Games

Google's frustrations in India stem from two factors. One is the red-hot job market in Indian tech. Engineering students are assured a job a year before they graduate. But Google makes things hard for itself by having some of the most exacting hiring standards going. The contest is an example. Participants are tested on aptitude in problem solving, on designing and writing code, and on testing peer-written work. Finalists are asked to create and test software for unique Web searches and to get from point A to B in a city with a minimum number

of turns. The final challenge is programming a war-based board game, a task so complex that only winner Poernomo completes it.

For Google, the Code Jam will serve as a short cut through its hiring regime. Candidates normally go through a seven-stage process that can last months—and, at the end of it, they're more likely to be rejected than hired. Much of that screening can be set aside for Code Jam winners.

For *Wunderkinder* like Poernomo, Google can be patient. Stanford grad Jon McAlister was the 2001 winner of TopCoder's U.S. Collegiate Code Jam, but didn't sign up with Google until 2004. He eventually rejected competing offers from Goldman, Sachs & Co. and Microsoft Corp. "Google is the genuine engineering company," says McAlister. Google hopes its India finalists think so, too.

Questions

1. How does Google ordinarily recruit and select new employees?
2. How do Code Jams short cut the typical recruitment and selection process?
3. What kind of testing takes place at Code Jams?
4. Why is Google willing to keep positions open for Code Jam winners, sometimes waiting a few years for them to eventually join the company?

Source: J. Puliyyenthuruthel, "How Google Searches—For Talent." Reprinted from the April 11, 2005, issue of *BusinessWeek* by special permission. Copyright © 2005 by the McGraw-Hill Companies, Inc.

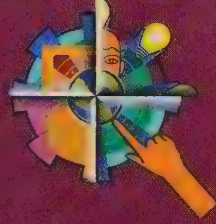
CHAPTER 13

Communication and Information Technology Management

Learning Objectives

After studying this chapter, you should be able to:

- Differentiate between data and information, list the attributes of useful information, and describe three reasons why managers must have access to information to perform their tasks and roles effectively.
- Explain why effective communication—the sharing of information—helps an organization gain a competitive advantage, and describe the communication process.
- Define information richness, and describe the information richness of communication media available to managers.
- Describe the computer hardware and software innovations that have created the information technology revolution.
- Differentiate among four kinds of management information systems.



Management Snapshot

Herman Miller's Office of the Future

How can managers create competitive advantage by using IT to improve communication?

In recent years, managers at Herman Miller have been finding countless ways to use IT and the Internet to give their company a competitive advantage over rival office furniture makers (OFMs) such as Steelcase and Hon.¹ From the beginning, like managers at the other OFMs, Miller's managers saw the potential of the Internet for selling Miller office furniture to potential business customers. The other companies' Web sites were online advertisements for their products, services, capabilities, and other relevant marketing and historical information. However, very quickly, managers realized the true potential of email both inside a company on its intranet and between companies over the Internet. In Herman Miller's case, the expanding use of the Internet to improve communication followed a definite pattern.

First, Miller's managers developed IT that linked all the company's dealers and salespeople to its manufacturing hub so that sales orders could be coordinated with the custom

design department and with manufacturing, enabling customers to receive pricing and scheduling information promptly. Then, with this customer delivery system in place, Miller developed IT to allow its manufacturing oper-



Herman Miller uses the Internet to reduce errors and time-to-market in delivering custom office furniture such as that depicted here.

ations to communicate with its network of suppliers so that its input supply chain would be coordinated with its customer needs.

Miller's managers noticed that the company's competitors moved quickly to imitate its IT, so Miller began to search for new ways to take advantage of the opportunities IT

offered. When they realized that IT could transform the office furniture business itself, they began to define Herman Miller as a “digital” enterprise. Infused with e-business, the company saw its mission as not just to improve efficiency by reducing costs but also to change the way the customer experienced “Herman Miller” and increase value for the customer. Miller’s managers accomplished this in several different ways.

One of their main Web initiatives was the establishment of an e-learning tool, Uknowit.com to communicate, which became Herman Miller’s online university. Via the Web thousands of Miller’s employees and dealers are currently enrolled in Uknowit.com, where they choose from 85 courses covering technology, products and services, product applications, consultative/selling skills, and industry competitive knowledge. The benefits to Miller, its dealers, and its customers from this IT communication initiative are improved speed to market and better ability to respond to competitors’ tactics. That is, salespeople and dealers now have the information and tools they need to compete for and keep customers. In the office furniture industry the average ramp-up time for a new sales associate is typically 24 to 36 months due to the complexity of the products and sales cycle/process. Utilizing e-learning has cut this time in half.

Moreover, the office furniture business offers highly customized solutions to its customers. A main source of competitive advantage is the ability to give customers exactly what they want and at the right price. Traditionally, the contract furniture industry had a hard time meeting deadlines for customized furniture solutions, and delivery to customers was often late. As a result of Miller’s new communication information systems, its salespeople are giving design and manufacturing more accurate and timely information, which has reduced the incidence of sales and specification errors during the selling process. Also, with the new systems time to market has been reduced, and Miller is committed to being able to offer customers highly customized furniture in 10 business days or less.

Of course, all these IT initiatives were costly to Herman Miller. Thousands of hours of management time have been spent developing the information systems and providing content, such as information on competitors for the company’s online classes. Herman Miller’s managers are looking at the long term; they believe they have created a real source of competitive advantage for their company that will sustain it in the years ahead.

Overview

Even with all the advances in information technology available to managers, ineffective communication continues to take place in organizations. Some managers recognize this problem and realize that IT is a tool to improve human communication, not a substitute for human communication. This is how managers at Herman Miller think about the way IT should be used. Those managers are emphasizing the humanization of IT and are striving to bring people back to the center stage of effective communication. Ineffective communication is detrimental for managers, workers, and organizations; it can lead to poor performance, strained interpersonal relations, poor service, and dissatisfied customers. Managers at all levels need to be good communicators in order for an organization to be effective and gain a competitive advantage.

In this chapter we survey information systems and information technology in general, looking at the relationship between information and the manager’s job. Then we describe the nature of communication and explain why it is so important for all managers and their subordinates to be effective communicators. We describe the communication media available to managers and the factors they need to

consider when selecting a communication medium for each message they send. We consider the communication networks that organizational members rely on, and we explore how advances in information technology have expanded managers' communication options.

Finally, we discuss several types of information systems that managers can use to help themselves perform their jobs, and we examine the impact that rapidly evolving information systems and technologies may have on managers' jobs and on an organization's competitive advantage. By the end of this chapter, you will understand the profound ways in which new developments in information systems and technology are shaping the way managers communicate and their functions and roles.

Information and the Manager's Job

data Raw, unsummarized, and unanalyzed facts.

information Data that is organized in a meaningful fashion.

Managers cannot plan, organize, lead, and control effectively unless they have access to information. Information is the source of the knowledge and intelligence that they need to make the right decisions. Information, however, is not the same as data.² **Data** is raw, unsummarized, and unanalyzed facts such as volume of sales, level of costs, or number of customers. **Information** is data that is organized in a meaningful fashion, such as in a graph showing changes in sales volume or costs over time. By itself, data does not tell managers anything; information, in contrast, can communicate a great deal of useful knowledge to the person who receives it—such as a manager who sees sales falling or costs rising. The distinction between data and information is important because one of the uses of information technology is to help managers transform data into information in order to make better managerial decisions.

Consider the case of a manager in a supermarket who must decide how much shelf space to allocate to two breakfast cereal brands for children: Dentist's Delight and Sugar Supreme. Most supermarkets use checkout scanners to record individual sales and store the data on a computer. Accessing this computer, the manager might find that Dentist's Delight sells 50 boxes per day and Sugar Supreme sells 25 boxes per day. This raw data, however, is of little help in assisting the manager to decide how to allocate shelf space. The manager also needs to know how much shelf space each cereal currently occupies and how much profit each cereal generates for the supermarket.

Suppose the manager discovers that Dentist's Delight occupies 10 feet of shelf space and Sugar Supreme occupies 4 feet and that Dentist's Delight generates 20 cents of profit a box while Sugar Supreme generates 40 cents of profit a box. By putting these three bits of data together (number of boxes sold, amount of shelf space, and profit per box), the manager gets some useful information on which to base a decision: Dentist's Delight generates \$1 of profit per foot of shelf space per day [(50 boxes @ \$.20)/10 feet], and Sugar Supreme generates \$2.50 of profit per foot of shelf space per day [(25 boxes @ \$.40)/4 feet]. Armed with this information, the manager might decide to allocate less shelf space to Dentist's Delight and more to Sugar Supreme.

Attributes of useful information

Four factors determine the usefulness of information to a manager: quality, timeliness, completeness, and relevance (see Figure 13.1).

Figure 13.1
Factors
Affecting the
Usefulness of
Information



QUALITY Accuracy and reliability determine the quality of information.³ The greater accuracy and reliability are, the higher is the quality of information. For an information system to work well, the information that it provides must be of high quality. If managers conclude that the quality of information provided by their information system is low, they are likely to lose confidence in the system and stop using it. Alternatively, if managers base decisions on low-quality information, poor and even disastrous decision making can result. For example, the partial meltdown of the nuclear reactor at Three Mile Island in Pennsylvania in 1979 was the result of poor information caused by an information system malfunction. The information system indicated to engineers controlling the reactor that there was enough water in the reactor core to cool the nuclear pile, although this was in fact not the case. The consequences included the partial meltdown of the reactor and the release of radioactive gas into the atmosphere.

TIMELINESS Information that is timely is available when it is needed for managerial action, not after the decision has been made. In today's rapidly changing world, the need for timely information often means that information must be available on a real-time basis.⁴ **Real-time information** is information that reflects current conditions. In an industry that experiences rapid changes, real-time information may need to be updated frequently.

**real-time
information**

Frequently updated information that reflects current conditions.

Airlines use real-time information about the number of flight bookings and about competitors' prices to adjust their prices on an hour-to-hour basis to maximize their revenues. Thus, for example, the fare for flights from New York to Seattle might change from one hour to the next as fares are reduced to fill empty seats and raised when most seats have been sold. Airlines use real-time information about reservations to adjust fares at the last possible moment to fill planes and maximize revenues. U.S. airlines make more than 80,000 fare changes each day.⁵ Obviously, the managers who make such pricing decisions need real-time information about the current state of demand in the marketplace.

COMPLETENESS Information that is complete gives managers all the information they need to exercise control, achieve coordination, or make an effective decision. Recall from Chapter 5, however, that managers rarely have access to complete information. Instead, because of uncertainty, ambiguity, and bounded rationality, they have to make do with incomplete information.⁶ One of the functions of information systems is to increase the completeness of the information that managers have at their disposal.

RELEVANCE Information that is relevant is useful and suits a manager's particular needs and circumstances. Irrelevant information is useless and may actually hurt the performance of a busy manager who has to spend valuable time determining whether information is relevant. Given the massive amounts of information that managers are now exposed to and humans' limited information-processing capabilities, the people who design information systems need to make sure that managers receive only relevant information.

Today, software agents are increasingly being used by managers to scan and sort incoming email and prioritize it. A software agent is a software program that can be used to perform simple tasks such as scanning incoming information for relevance, taking some of the burden away from managers. Moreover, by recording and analyzing a manager's own efforts to prioritize incoming information, the software agent can mimic the manager's preferences and thus perform such tasks more effectively. For example, the software agent can automatically reprogram itself to place incoming email from the manager's boss at the top of the pile.⁷

Information systems and technology

information

system A system for acquiring, organizing, storing, manipulating, and transmitting information.

management information

system An information system that managers plan and design to provide themselves with the specific information they need.

information

technology The means by which information is acquired, organized, stored, manipulated, and transmitted.

An **information system** is a system for acquiring, organizing, storing, manipulating, and transmitting information.⁸ A **management information system (MIS)** is an information system that managers plan and design to provide themselves with the specific information they need to perform their roles effectively. Information systems have existed for as long as there have been organizations—a long time indeed. Before the computer age, most information systems were paper based: Clerks recorded important information on documents (often in duplicate or triplicate) in the form of words and numbers, sent a copy of the document to superiors, customers, or suppliers, as the case might be, and stored other copies in files for future reference.

Information technology is the means by which information is acquired, organized, stored, manipulated, and transmitted. Rapid advances in the power of information technology—specifically, through the use of computers—are having a fundamental impact on information systems and on managers, their organizations, and their suppliers and customers.⁹ So important are these advances in information technology that organizations that do not adopt new information technology, or adopt it ineffectively, will become uncompetitive with those that put it to good use.¹⁰ An interesting illustration of this can be found by comparing the on-line shopping information system of Amazon.com with that of Walmart.com and Bluelight.com (Kmart's on-line store).

Information Technology Byte

E-Stores: Amazon.com versus Bluelight.com versus Walmart.com

On-line stores live or die by their ability to provide customers with a satisfying shopping experience. Hundreds of now defunct dot-coms learned this lesson in the early 2000s when an inability to generate revenue from customers caused their collapse. Among dot-com survivors, however, the different shopping experiences provide an interesting comparison. Amazon.com began as a virtual on-line enterprise; Bluelight.com and Walmart.com were outcomes of their bricks-and-mortar parents' desire to experiment with on-line retailing.

Amazon.com was the first of these on-line stores to be up and running; from the beginning its storefront was designed with the Internet in mind. Bluelight.com was next, and Walmart.com was last. Walmart.com had an inauspicious beginning. Soon after it was up and running, it was suddenly shut down for six months while its information systems were reworked to make them user-friendly. A close look at the three companies' Web sites reveals major differences in the ways their virtual information systems operate. (Take the opportunity to examine these Web sites now.)

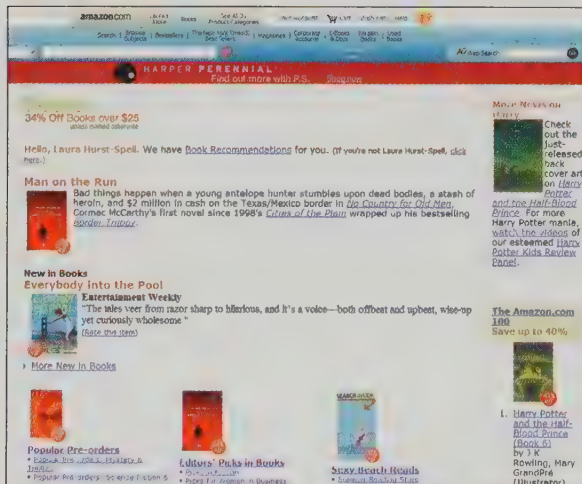
Amazon.com's Web site possesses the IT most interactive with its customers. Its information systems remember customers' preferences, the items they have viewed, and their past purchases; therefore, the systems can suggest related items that a customer might wish to consider purchasing, given what seem to be his or her lifestyle preferences. In addition, Amazon.com's customers can write reviews of its books and other products, and in this way they can talk among themselves and develop a more satisfying shopping experience. By contrast, Bluelight.com's

information system has some limited ability to suggest items that a customer might consider purchasing but has no "customer history" to build the shopping experience, and Walmart.com's system simply brings into view items that a customer selects from the various product categories and has no ability to provide a customized shopping experience. Another major difference among these on-line stores is in the convenience of the checkout process.¹¹ Once again Amazon.com wins out with its "one-click" technology, although other stores have imitated this.

These basic differences in information systems design are reflected in the degree to which customers make use of these on-line stores. Amazon.com is the most-visited on-line store by far, and Bluelight.com is much more popular than Walmart.com. Thus, it seems that the ability of managers to create the IT

that best meets the needs of their customers is a key determinant of the relative efficiency and effectiveness of these rival virtual businesses.

Managers need information for three reasons: to make effective decisions; to control the activities of the organization; and to coordinate the activities of the organization. We now examine these uses of information in detail.



Amazon.com is widely regarded as having the best, most customer-responsive Internet storefront in the business.

Information and decision making

Much of management (planning, organizing, leading, and controlling) is about making decisions. The marketing manager must decide what price to charge for a product, what distribution channels to use, and what promotional messages to emphasize. The manufacturing manager must decide how much of a product to make and how to make it. The purchasing manager must decide from whom to purchase inputs and what inventory of inputs to hold. The human relations manager must decide how much employees should be paid, how they should be trained, and what benefits they should be given. The engineering manager must make decisions about new product design. Top managers must decide how to allocate scarce financial resources among competing projects, how best to structure and control the organization, and what business-level strategy the organization should be pursuing. And, regardless of their functional orientation, all managers have to make decisions about matters such as what performance evaluation to give to a subordinate.

Decision making cannot be effective in an information vacuum. To make effective decisions, managers need information, both from inside the organization and from external stakeholders. When deciding how to price a product, for example, the marketing manager needs information about how consumers will react to different prices. She needs information about unit costs because she does not want to set the price below the costs of production. And she needs information about competitive strategy, since pricing strategy should be consistent with an organization's competitive strategy. Some of this information will come from outside the organization (for example, from consumer surveys) and some from inside the organization (information about unit production costs comes from manufacturing). As this example suggests, managers' ability to make effective decisions rests on their ability to acquire and process information.

Information and control

As discussed in Chapter 8, controlling is the process whereby managers regulate how efficiently and effectively an organization and its members are performing the activities necessary to achieve organizational goals.¹² Managers achieve control over organizational activities by taking four steps (see Figure 8.2): (1) They establish measurable standards of performance or goals. (2) They measure actual performance. (3) They compare actual performance against established goals. (4) They evaluate the result and take corrective action if necessary.¹³ Airborne Express, for example, has a delivery goal: to deliver by noon tomorrow 95 percent of the packages it picks up today. Throughout the United States, Airborne has a thousand ground stations (branch offices that coordinate the pickup and delivery of packages in a particular area) that are responsible for the physical pickup and delivery of packages. Airborne managers monitor the delivery performance of these stations on a regular basis; if they find that the 95 percent goal is not being attained, they determine why and take corrective action if necessary.¹⁴

To achieve control over any organizational activity, managers must have information. To control a ground station, a manager at Airborne needs to know how many of that station's packages are being delivered by noon. To get this information, the manager needs to make sure that an information system is in place. Packages to be shipped by Airborne are scanned with a hand-held scanner by the Airborne Express driver who first picks them up. The pickup information is sent by

a wireless link to a central computer at Airborne's Seattle headquarters. The packages are scanned again by the truck driver when they are delivered. The delivery information is also transmitted to Airborne's central computer. By accessing the central computer, a manager can quickly find out not only what percentage of packages are delivered by noon of the day after they were picked up but also how this information breaks down on a station-by-station basis.¹⁵

Management information systems, discussed later in the chapter, are used to control a variety of operations within organizations. In accounting, for example, information systems can be used to monitor expenditures and compare them against budgets.¹⁶ To track expenditures against budgets, managers need information on current expenditures broken down by relevant organizational units. Accounting information systems are designed to provide managers with such information. Another example of an information system used to monitor and control the daily activities of employees is the on-line MBO information system used by T. J. Rodgers at Cypress Semiconductor, discussed in Chapter 8. Rodgers implemented a computer-based information system that allows him to review the goals of all his employees in about four hours.¹⁷

Information and coordination

Coordinating department and divisional activities to achieve organizational goals is another basic task of management. As an extreme example of the size of the coordination task that managers face, consider the coordination effort involved in building Boeing's new commercial jet aircraft, the 777. The 777 is composed of 3 million individual parts and thousands of major components. Managers at Boeing have to coordinate the production and delivery of these parts so that they all arrive at Boeing's Everett, Washington, facility exactly when they are needed (for example, they want the wings to arrive before the engines). Boeing managers jokingly refer to this task as "coordinating 3 million parts in flying formation." To achieve this high level of coordination, managers need information about which supplier is producing what, when it is to be produced, and when it is to be delivered. Managers also need this information so that they are able to track the delivery performance of suppliers against expectations and receive advance warning of any likely problems. To meet these needs, managers at Boeing established a computer-based information system that links Boeing to all its suppliers and can track the flow of 3 million component parts through the production process—an immense task.

As noted in previous chapters, the coordination problems that managers face in managing their global supply chains to take advantage of national differences in the costs of production are increasing. To deal with global coordination problems, managers have been adopting sophisticated computer-based information systems that help them coordinate the flow of materials, semifinished goods, and finished products around the world.

communication

The sharing of information between two or more individuals or groups to reach a common understanding.

Communication, Information, and Management

Communication is the sharing of information between two or more people or groups to reach a common understanding.¹⁸ The "Management Snapshot" that opens this chapter highlights some important aspects of this definition. First and foremost, communication, no matter how

electronically based, is a human endeavor and involves individuals and groups. Second, communication does not take place unless a common understanding is reached. Thus, if you try to call a business to speak to a person in customer service or billing and you are bounced back and forth between endless automated messages and menu options and eventually hang up in frustration, communication has not taken place.

The importance of good communication

In Chapter 1, we described how in order for an organization to gain a competitive advantage, managers must strive to increase efficiency, quality, responsiveness to customers, and innovation. Good communication is essential for attaining each of these four goals and thus is a necessity for gaining a competitive advantage.

Managers can *increase efficiency* by updating the production process to take advantage of new and more efficient technologies and by training workers to operate the new technologies and expand their skills. Good communication is necessary for managers to learn about new technologies, implement them in their organizations, and train workers in how to use them. Similarly, *improving quality* hinges on effective communication. Managers need to communicate to all members of an organization the meaning and importance of high quality and the routes to attaining it. Subordinates need to communicate quality problems and suggestions for increasing quality to their superiors, and members of self-managed work teams need to share their ideas for improving quality with each other.

Good communication can also help to increase *responsiveness to customers*. When the organizational members who are closest to customers, such as salespeople in department stores and tellers in banks, are empowered to communicate customers' needs and desires to managers, managers are better able to respond to these needs. Managers, in turn, must communicate with other organizational members to determine how best to respond to changing customer preferences.

Innovation, which often takes place in cross-functional teams, also requires effective communication. Members of a cross-functional team developing a new kind of compact disc player, for example, must communicate effectively with each other to develop a disc player that customers will want, that will be of high quality, and that can be produced efficiently. Members of the team also must communicate with managers to secure the resources they need to develop the disc player and keep the managers informed of progress on the project.

Effective communication is necessary for managers and all members of an organization to increase efficiency, quality, responsiveness to customers, and innovation and thus gain a competitive advantage for their organization. Managers therefore must have a good understanding of the communication process if they are to perform effectively. Collaboration software is IT that aims to promote highly interdependent interactions among members of a team and provide the team with an electronic meeting site for communication.¹⁹ For work that is truly team-based, entails a number of highly interdependent yet distinct components, and involves team members with distinct areas of expertise who need to closely coordinate their efforts, collaboration software can be a powerful communication tool, as profiled in the following "Information Technology Byte."



Information Technology Byte

Collaboration Software Facilitates Communication in Teams

Collaboration software provides members of a team with an on-line work site where they can post, share, and save data, reports, sketches, and other documents; keep calendars; have team-based online conferences; and send and receive messages. The software can also keep and update progress reports, survey team members about different issues, forward documents to managers, and let users know which of their team members are also online and at the site.²⁰ Having an integrated on-line work area can help to organize and centralize the work of a team, help to ensure that information is readily available as needed, and also help team members to make sure that important information is not overlooked. Collaboration software can be much more efficient than email or instant messaging for managing ongoing team collaboration and interaction that is not face-to-face. Moreover, when a team does meet face-to-face, all documents the team might need in the course of the meeting are just a click away.²¹

The New York-based public relations company Ketchum Inc. uses collaboration software for some of its projects. For example, Ketchum is managing public relations, marketing, and advertising for a new charitable program that Fireman's Fund Insurance Co. has undertaken. By using the eRoom software provided by Documentum (a part of EMC Corporation), Ketchum employees working on the project at six different locations, employee representatives from Fireman's, and a graphics company that is designing a Web site for the program can share plans, documents, graphic designs, and calendars at an online work site.²² Members of the Ketchum-Fireman team get email alerts when something has been modified or added to the site. As Ketchum's chief information officer Andy Roach puts it, "The fact that everyone has access to the same document means Ketchum isn't going to waste time on the logistics and can focus on the creative side."²³

Another company taking advantage of collaboration software is Honeywell International Inc. Managers at Honeywell decided to use the SharePoint collaboration software provided by Microsoft, in part because it can be integrated with other Microsoft software such as Outlook. So, for example, if a team using SharePoint makes a change to the team's calendar, that change will be automatically made in team members' Outlook calendars.²⁴ Clearly, collaboration software has the potential to enhance communication efficiency and effectiveness in teams.

The communication process

sender The person or group wishing to share information.

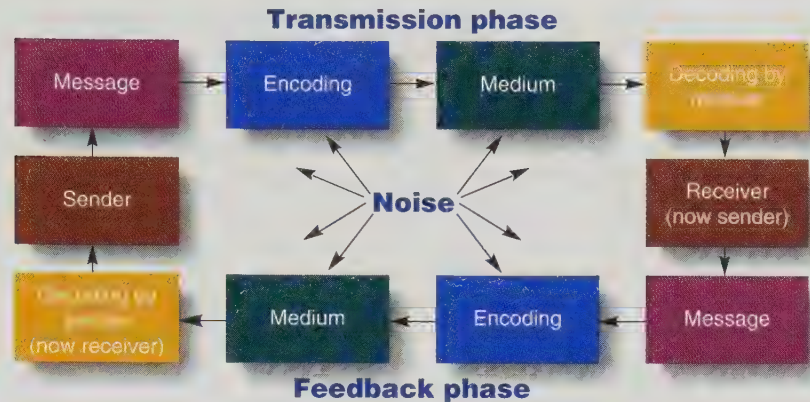
message

The information that a sender wants to share.

The communication process consists of two phases. In the *transmission phase*, information is shared between two or more individuals or groups. In the *feedback phase*, a common understanding is assured. In both phases, a number of distinct stages must occur for communication to take place (see Figure 13.2).²⁵

Starting the transmission phase, the **sender**, the person or group wishing to share information with some other person or group, decides on the **message**, what

Figure 13.2
The
Communication
Process



encoding Translating a message into understandable symbols or language.

noise Anything that hampers any stage of the communication process.

receiver The person or group for which a message is intended.

medium The pathway through which an encoded message is transmitted to a receiver.

decoding Interpreting and trying to make sense of a message.

verbal communication The encoding of messages into words, either written or spoken.

nonverbal communication The encoding of messages by means of facial expressions, body language, and styles of dress.

information to communicate. Then the sender translates the message into symbols or language, a process called **encoding**; often messages are encoded into words. **Noise** is a general term that refers to anything that hampers any stage of the communication process.

Once encoded, a message is transmitted through a medium to the **receiver**, the person or group for which the message is intended. A **medium** is simply the pathway, such as a phone call, a letter, a memo, or face-to-face communication in a meeting, through which an encoded message is transmitted to a receiver. At the next stage, the receiver interprets and tries to make sense of the message, a process called **decoding**. This is a critical point in communication.

The feedback phase is initiated by the receiver (who becomes a sender). The receiver decides what message to send to the original sender (who becomes a receiver), encodes it, and transmits it through a chosen medium (see Figure 13.2). The message might contain a confirmation that the original message was received and understood or a restatement of the original message to make sure that it has been correctly interpreted; or it might include a request for more information. The original sender decodes the message and makes sure that a common understanding has been reached. If the original sender determines that a common understanding has not been reached, sender and receiver cycle through the whole process as many times as are needed to reach a common understanding.

The encoding of messages into words, written or spoken, is **verbal communication**. We also encode messages without using written or spoken language. **Nonverbal communication** shares information by means of facial expressions (smiling, raising an eyebrow, frowning, dropping one's jaw), body language (posture, gestures, nods, shrugs), and even style of dress (casual, formal, conservative, trendy). For example, to communicate or signal that General Motors' old bureaucracy has been dismantled and the company is decentralized and more informal than it used to be, top managers at GM wear slacks and sport jackets rather than business suits when they walk around GM plants.²⁶ The trend toward increasing empowerment of the workforce has led GM and other managers to dress informally to communicate that all employees of an organization are team members, working together to create value for customers.

Nonverbal communication can be used to back up or reinforce verbal communication. Just as a warm and genuine smile can back up words of appreciation

for a job well done, a concerned facial expression can back up words of sympathy for a personal problem. In such cases, the congruence between verbal and nonverbal communication helps to ensure that a common understanding is reached.

Sometimes when members of an organization decide not to express a message verbally, they inadvertently do so nonverbally. People tend to have less control over nonverbal communication, and often a verbal message that is withheld gets expressed through body language or facial expressions. A manager who agrees to a proposal that she or he actually is not in favor of may unintentionally communicate disfavor by grimacing.

Sometimes nonverbal communication is used to send messages that cannot be sent through verbal channels. Many lawyers are well aware of this communication tactic. Lawyers are often schooled in techniques of nonverbal communication such as choosing where to stand in the courtroom for maximum effect and using eye contact during different stages of a trial. Lawyers sometimes get into trouble for using inappropriate nonverbal communication in an attempt to influence juries. In a Louisiana court, prosecuting attorney Thomas Pirtle was admonished and fined \$2,500 by Judge Yada Magee for shaking his head in an expression of doubt, waving his arms indicating disfavor, and chuckling when attorneys for the defense were stating their case.²⁷

The dangers of ineffective communication

Because managers must communicate with others to perform their various roles and tasks, managers spend most of their time communicating, whether in meetings, in telephone conversations, through email, or in face-to-face interactions. Indeed, some experts estimate that managers spend approximately 85 percent of their time engaged in some form of communication.²⁸ Effective communication is so important that managers cannot just be concerned that they themselves are effective communicators; they also have to help their subordinates be effective communicators. When all members of an organization are able to communicate effectively with each other and with people outside the organization, the organization is much more likely to perform highly and gain a competitive advantage.

When managers and other members of an organization are ineffective communicators, organizational performance suffers, and any competitive advantage the organization might have is likely to be lost. Moreover, poor communication sometimes can be downright dangerous and even lead to tragic and unnecessary loss of human life. For example, researchers from Harvard University studied the causes of mistakes, such as a patient receiving the wrong medication, in two large hospitals in the Boston area. They discovered that some mistakes in hospitals occur because of communication problems—physicians not having the information they need to correctly order medications for their patients or nurses not having the information they need to correctly administer medications. The researchers concluded that some of the responsibility for these mistakes lies with hospital management, which has not taken active steps to improve communication.²⁹

Communication problems in the cockpit of airplanes and between flying crews and air traffic controllers are unfortunately all too common, sometimes with deadly

consequences. In the late 1970s, two jets collided in Tenerife (one of the Canary Islands) because of miscommunication between a pilot and the control tower, and 600 people were killed. The tower radioed to the pilot, "Clipper 1736 report clear of runway." The pilot mistakenly interpreted this message to mean that he was cleared for takeoff.³⁰ Unfortunately, errors like this one are not a thing of the past. A safety group at NASA tracked over 6,000 unsafe flying incidents and found that communication difficulties caused approximately 529 of them.³¹

Information Richness and Communication Media

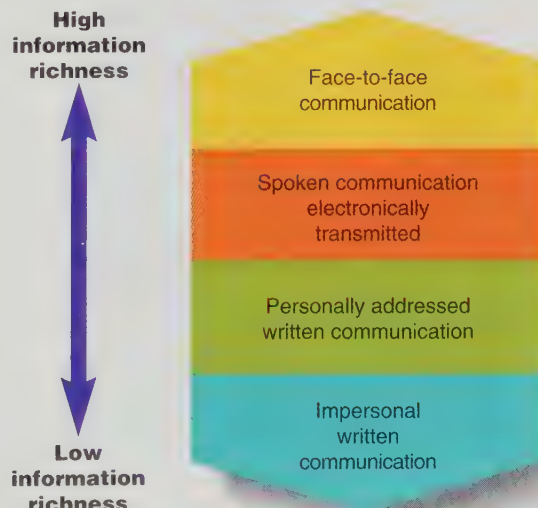
information richness The amount of information that a communication medium can carry and the extent to which the medium enables the sender and receiver to reach a common understanding.

To be effective communicators, managers (and other members of an organization) need to select an appropriate communication medium for *each* message they send. Should a change in procedures be communicated to subordinates in a memo sent through email? Should a congratulatory message about a major accomplishment be communicated in a letter, in a phone call, or over lunch? Should a layoff announcement be made in a memo or at a plant meeting?

Should the members of a purchasing team travel to Europe to cement a major agreement with a new supplier, or should they do so through faxes? Managers deal with these questions day in and day out.

There is no one best communication medium for managers to rely on. In choosing a communication medium for any message, managers need to consider three factors. The first and most important is the level of information richness that is needed. **Information richness** is the amount of information a communication medium can carry and the extent to which the medium enables the sender and receiver to reach a common understanding.³² The communication media that managers use vary in their information richness (see Figure 13.3).³³ Media high in information richness are able to carry an extensive amount of information and generally enable receivers and senders to come to a common understanding.

Figure 13.3
The Information Richness of Communication Media



The second factor that managers need to take into account in selecting a communication medium is the *time* needed for communication, because managers' and other organizational members' time is valuable. Managers at United Parcel Service, for example, dramatically reduced the amount of time they spent by using videoconferences instead of face-to-face communication, which required managers to travel overseas.³⁴

The third factor that affects the choice of a communication medium is the *need for a paper or electronic trail* or some kind of written documentation that a message was sent and received. A manager may wish to document in writing, for example, that a subordinate was given a formal warning about excessive lateness.

In the remainder of this section we examine four types of communication media that vary along the three dimensions of information richness, time, and the availability of a paper or electronic trail.³⁵

Face-to-face communication

Face-to-face communication is the medium that is highest in information richness. When managers communicate face-to-face, they not only can take advantage of verbal communication but they also can interpret each other's nonverbal signals such as facial expressions and body language. A look of concern or puzzlement can sometimes tell more than a thousand words, and managers can respond to these nonverbal signals on the spot. Face-to-face communication also enables managers to receive instant feedback. Points of confusion, ambiguity, or misunderstanding can be resolved, and managers can cycle through the communication process as many times as they need to, to reach a common understanding.

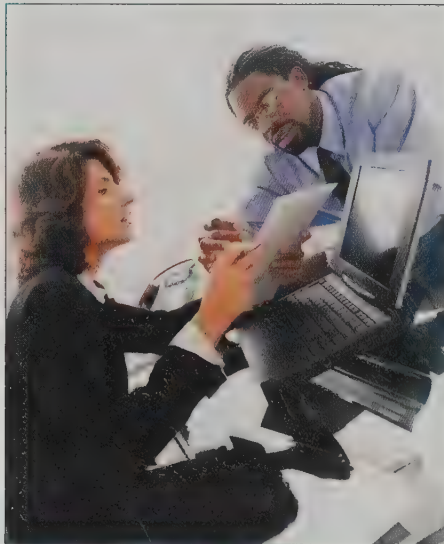
Management by wandering around is a face-to-face communication technique that is effective for many managers at all levels in an organization.³⁶

Rather than scheduling formal meetings with subordinates, managers walk around work areas and talk informally with employees about issues and concerns that both employees and managers may have. These informal conversations provide managers and subordinates with important information and at the same time foster the development of positive relationships. William Hewlett and David Packard, founders and former top managers of Hewlett-Packard, found management by wandering around a highly effective way to communicate with their employees.

Because face-to-face communication is highest in information richness, you might think that it should always be the medium of choice for managers. This is not the case, however, because of the amount of time it takes and the lack of a paper or electronic trail resulting

management by wandering around

A face-to-face communication technique in which a manager walks around a work area and talks informally with employees about issues and concerns.



In spite of the popularity of electronic communication, face-to-face communication is still the medium that is highest in information richness.

from it. For messages that are important, personal, or likely to be misunderstood, it is often well worth managers' time to use face-to-face communication and, if need be, supplement it with some form of written communication documenting the message.

Advances in information technology are providing managers with new and close alternative communication media for face-to-face communication. Many organizations such as American Greetings Corp. and Hewlett-Packard are using *videoconferences* to capture some of the advantages of face-to-face communication (such as access to facial expressions) while saving time and money because managers in different locations do not have to travel to meet with one another. During a videoconference, managers in two or more locations communicate with each other over large TV or video screens; they not only hear each other but also see each other throughout the meeting.

In addition to saving travel costs, videoconferences sometimes have other advantages. Managers at American Greetings have found that decisions get made more quickly when videoconferences are used, because more managers can be involved in the decision-making process and therefore fewer managers have to be consulted outside the meeting itself. Managers at Hewlett-Packard have found that videoconferences have shortened new product development time by 30 percent for similar reasons. Videoconferences also seem to lead to more efficient meetings. Some managers have found that their meetings are 20 to 30 percent shorter when videoconferences are used instead of face-to-face meetings.³⁷

Taking videoconferences one step further, IBM and TelePort Corporation have joined forces to build virtual dining rooms in which top managers can actually have power meals with other managers in another location. Managers in one location are seated around a large, round table bisected by a huge video screen on which they are able to see (life-size) their dining partners in another location sitting around the same kind of table having the same kind of meal. Even though managers may be hundreds or thousands of miles apart, they can eat together as they discuss pressing concerns. The cameras enabling the transmission of the video images are hidden in flower arrangements so as not to unnerve the diners. The tables start at \$150,000, and major hotel chains such as Hilton, Hyatt, and Doubletree are interested in purchasing them for use by their business customers.³⁸

Spoken communication electronically transmitted

After face-to-face communication, spoken communication electronically transmitted over phone lines is second highest in information richness (see Figure 13.2). Although managers communicating over the telephone do not have access to body language and facial expressions, they do have access to the tone of voice in which a message is delivered, the parts of the message the sender emphasizes, and the general manner in which the message is spoken, in addition to the actual words themselves. Thus, telephone conversations have the capacity to convey extensive amounts of information. Managers also can ensure that mutual understanding is reached because they can get quick feedback over the phone and answer questions.

Voice mail systems and answering machines also allow managers to send and receive verbal electronic messages over telephone lines. Voice mail systems are companywide systems that enable senders to record messages for members of an organization who are away from their desks and allow receivers to access their messages when hundreds of miles away from the office. Such systems are obviously a necessity when managers are frequently out of the office, and managers on the road are well advised to periodically check their voice mail.

Personally addressed written communication

Lower than electronically transmitted verbal communication in information richness is personally addressed written communication (see Figure 13.2). One of the advantages of face-to-face communication and verbal communication electronically transmitted is that they both tend to demand attention, which helps ensure that receivers pay attention. Personally addressed written communications such as memos and letters also have this advantage. Because they are addressed to a particular person, the chances are good that the person will actually pay attention to (and read) them. Moreover, the sender can write the message in a way that the receiver is most likely to understand. Like voice mail, written communication does not enable a receiver to have his or her questions answered immediately, but when messages are clearly written and feedback is provided, common understandings can still be reached.

Even if managers use face-to-face communication, a follow-up in writing is often needed for messages that are important or complicated and need to be referred to later. This is precisely what Karen Stracker, a hospital administrator, did when she needed to tell one of her subordinates about an important change in the way the hospital would be handling denials of insurance benefits. Stracker met with the subordinate and described the changes face-to-face. Once she was sure that the subordinate understood them, she handed her a sheet of instructions to follow, which essentially summarized the information they had discussed.

Email also fits into this category of communication media because senders and receivers are communicating through personally addressed written words. The words, however, are appearing on their personal computer screens rather than on pieces of paper. Email is becoming so widespread in the business world that managers are even developing their own email etiquette. To save time, Andrew Giangola, a manager at Simon & Schuster, a book publisher, used to type all his email messages in capital letters. He was surprised when a receiver of one of his messages responded, "Why are you screaming at me?" Messages in capital letters are often perceived as being shouted or screamed, and thus Giangola's routine use of capital letters was bad email etiquette. Here are some other guidelines from polite emailers: Always punctuate messages; do not ramble on or say more than you need to; do not act as though you do not understand something when in fact you do understand it; and pay attention to spelling and format (put a memo in memo form). To avoid embarrassments like Giangola's, managers at Simon & Schuster created a task force to develop guidelines for email etiquette.³⁹

The growing popularity of email has also enabled many workers and managers to become telecommuters, people who are employed by organizations and work out of offices in their own homes. There are approximately 8.4 million telecommuters

in the United States. Many telecommuters indicate that the flexibility of working at home enables them to be more productive while giving them a chance to be closer to their families and not waste time traveling to and from the office.⁴⁰ A study conducted by Georgetown University found that 75 percent of the telecommuters surveyed said their productivity increased and 83 percent said their home life improved once they started telecommuting.⁴¹

Unfortunately, the growing use of email has been accompanied by growing abuse of email. Some employees sexually harass co-workers through email, and divorcing spouses who work together sometimes sign their spouse's name to email and send insulting or derogatory messages to the spouse's boss. Robert Mirguet, information systems manager at Eastman Kodak, has indicated that some Kodak employees have used Kodak's email system to try to start their own businesses during working hours. Kodak managers monitor employees' email messages when they suspect some form of abuse. Top managers also complain that sometimes their email is clogged with junk mail. In a recent survey over half of the organizations contacted acknowledged some problems with their email systems.⁴²

To avoid these and other costly forms of email abuse, managers need to develop a clear policy specifying what company email can and should be used for and what is out of bounds. Managers also should clearly communicate this policy to all members of an organization, as well as the procedures that will be used when email abuse is suspected and the consequences that will result when email abuse is confirmed.

Impersonal written communication

Impersonal written communication is lowest in information richness and is well suited for messages that need to reach a large number of receivers. Because such messages are not addressed to particular receivers, feedback is unlikely, so managers must make sure that messages sent by this medium are written clearly in language that all receivers will understand.

Managers often find company newsletters useful vehicles for reaching large numbers of employees. Many managers give their newsletters catchy names to spark employee interest and also to inject a bit of humor into the workplace. Managers at the pork-sausage maker Bob Evans Farms Inc. called their newsletter "The Squealer" for many years but recently changed the title to "The Homesteader" to reflect the company's broadened line of products. Managers at American Greetings Corp., at Yokohama Tire Corp., and at Eastman Kodak call their newsletters "Expressions," "TreadLines," and "Kodakery," respectively. Managers at Quaker State Corp. held a contest to rename their newsletter. Among the 1,000 submitted names were "The Big Q Review," "The Pipeline," and "Q. S. Oil Press"; the winner was "On Q."⁴³

Managers can use impersonal written communication for various types of messages, including rules, regulations, policies, newsworthy information, and announcements of changes in procedures or the arrival of new organizational members. Impersonal written communication also can be used to communicate instructions about how to use machinery or how to process work orders or customer requests. For these kinds of messages, the paper or electronic trail left by this communication medium can be invaluable for employees.

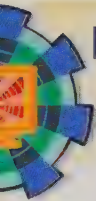
Like personal written communication, impersonal written communication can be delivered and retrieved electronically, and this is increasingly being done in

information overload

A superabundance of information that increases the likelihood that important information is ignored or overlooked and tangential information receives attention.

companies large and small. Unfortunately, the ease with which electronic messages can be spread has led to their proliferation. The electronic inboxes of many managers and workers are backlogged, and they rarely have time to read all the electronic work-related information available to them. The problem with such **information overload**—a superabundance of information—is the potential for important information to be ignored or overlooked while tangential information receives attention. Moreover, information overload can result in thousands of hours and millions in dollars in lost productivity.

Realizing the hazards of overload, Nathan Zeldes, computing productivity manager for Intel's division in Israel, decided to tackle this problem head-on.⁴⁴ In Zeldes's division, some 3 million emails are sent or received each day, and some employees receive more than 300 messages a day. On average, employees spend around two and a half hours a day dealing with this barrage of information. To combat this problem, Zeldes developed a training program to educate employees about how email can improve productivity and how it can be used in ways that limit overload. Reactions to the training program have been positive, and it is now used in Intel divisions around the globe.⁴⁵ Some of Intel's organizational learning about email and overload is captured in the company's "10 Commandments of Email," reproduced in the following "Information Technology Byte."



Information Technology Byte

Intel's "10 Commandments of Email"

1. Don't use your inbox as a catchall folder for everything you need to work on. Read items once, and answer them immediately if necessary, delete them if possible, or move them to project-specific folders.
2. Set up a "Five Weeks Folder" that deletes its content automatically after five weeks. Use it as a repository for messages you're unsure about, such as that email you want to delete, but you're not sure if the guy's going to call you tomorrow and ask you about it.
3. Assist colleagues' inbox-filtering efforts by agreeing on acronyms to use in subject lines that quickly identify action items and other important messages. Sample acronyms: <AR>, Action Required; <MSR>, Monthly Status Report.
4. Send group mail only when it is useful to *all* recipients. Use "reply-to-all" and "CC:" buttons sparingly.
5. Ask to be removed from distribution lists that you don't need to be on.
6. To cut down on pileup, use the "out-of-office" feature of your email, in addition to your voice mail, to notify people when you are traveling.
7. When possible, send a message that is only a subject line, so recipients don't have to open the email to read a single line. End the subject line with <EOM>, the acronym for End of Message.
8. Graphics and attachments are fun, but they slow down your ability to download messages when you're on the road. Use them sparingly.
9. If you're sending an attachment larger than 5 MB to a large group of recipients, consider putting it on the company's Web site or intranet instead.
10. Be specific. If you send a 20-page attachment, tell the recipient that the important information is on pages 2 and 17.⁴⁶

The Information Technology Revolution

Computer-based information technology can greatly facilitate and improve the communication process. It has allowed managers to develop computer-based management information systems that provide timely, complete, relevant, and high-quality information. As we have discussed, IT allows companies to improve their responsiveness to customers, minimize costs, and thus improve their competitive position. The link between information systems, communication, and competitive position is an important one that may determine the success or failure of organizations in an increasingly competitive global environment. To better explain the current revolution in information technology, in this section we examine several key aspects of computer-based information technology.

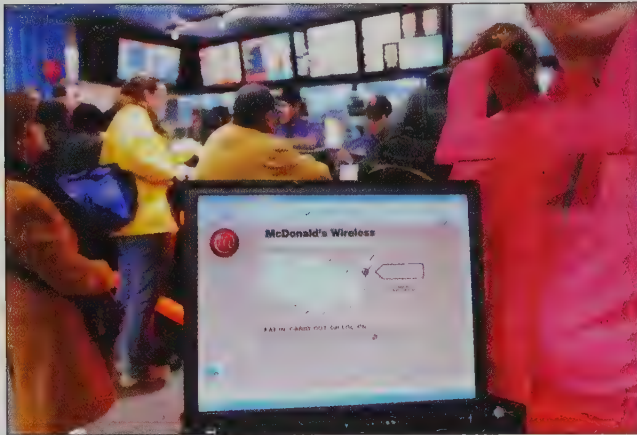
The tumbling price of information

The information technology revolution began with the development of the first computers—the hardware of computer-based information technology—in the 1950s. The language of computers is a digital language of zeros and ones. Words, numbers, images, and sounds can all be expressed in zeros and ones. Each letter in the alphabet has its own unique code of zeros and ones, as does each number, each color, and each sound. For example, the digital code for the number 20 is 10100. In the language of computers it takes a lot of zeros and ones to express even a simple sentence, to say nothing of complex color graphics or moving video images. Nevertheless, modern computers can read, process, and store millions of instructions per second (an instruction is a line of software code) and thus vast amounts of zeros and ones. It is this awesome power that forms the foundation of the current information technology revolution.

The brains of modern computers are microprocessors (Intel's Pentium chips and its newest chip, the Itanium chip, are microprocessors). Between 1991 and 2001, the relative cost of computer processing fell so dramatically that Gordon Moore, a computer guru, noted that "If the auto industry advanced as rapidly as the semiconductor industry, a Rolls Royce would get a half a million miles per gallon, and it would be cheaper to throw it away than to park it."⁴⁷ As the costs of acquiring, organizing, storing, and transmitting information have tumbled, computers have become almost as common as wireless phones and microwaves.⁴⁸ In addition, advances in microprocessor technology have led to dramatic reductions in the cost of communication between computers, which also have contributed to the falling price of information and information systems.

Wireless communications

Another trend of considerable significance for information systems has been the rapid growth of wireless communication technologies, particularly digital communications. Wireless service was first offered in the United States in 1983. Initially, growth was slow, but since 1990 wireless service has spread rapidly. In 1984, there were 100,000 cellular subscribers in the United States;⁴⁹ in 1994, 16 million; by 2001, 110 million.⁵⁰ Some experts predict that worldwide subscribership will reach 1.2 billion people by 2006.⁵¹



A “mobile messenger” holds a laptop computer featuring the new wireless computer connection at a McDonald’s restaurant in New York City. In 2003, McDonald’s launched a major wireless Internet rollout in New York City and in three major U.S. markets.

Wireless communication is significant for the information technology revolution because it facilitates the linking together of computers, which greatly increases their power and adaptability. It is already possible to purchase a battery-operated laptop computer that has a wireless modem built in to facilitate communication with a “home” computer. An engineer or salesperson working in the field can send information to, and receive information from, the home office by using the wireless capabilities built into computers. Because a computer no longer has to be plugged into a hard-wired telephone line, accessing a large computer-based information system is much easier than it used to be.

Computer networks

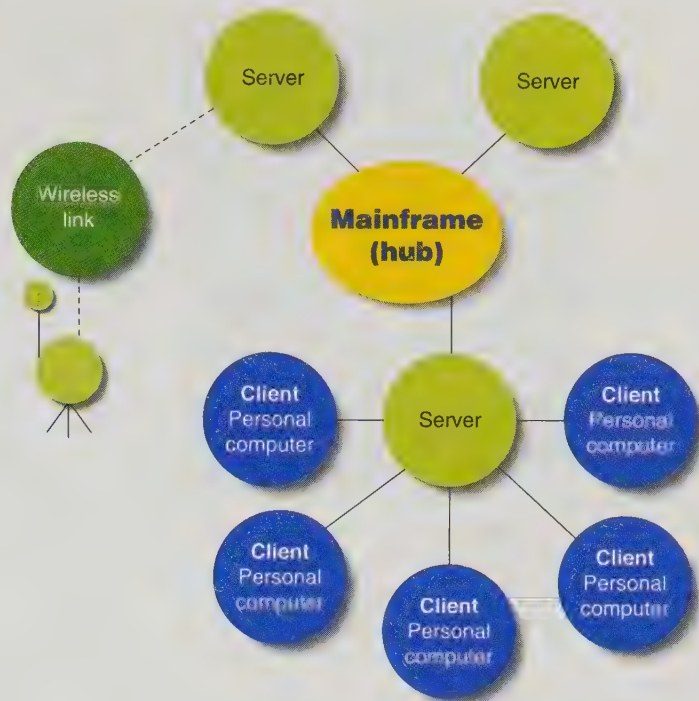
networking The exchange of information through a group or network of interlinked computers.

The tumbling price of computing power and information and the use of wireless communication channels have facilitated **networking**, the exchange of information through a group or network of interlinked computers. The most common arrangement now emerging is a three-tier network consisting of clients, servers, and a mainframe (see Figure 13.4). At the outer nodes of a typical three-tier network are the personal computers (PCs) that sit on the desks of individual users. These personal computers, referred to as *clients*, are linked to a local *server*, a high-powered midrange computer that “serves” the client personal computers. Servers often store power-hungry software programs that can be run more effectively on a server than on individuals’ personal computers. Servers may also manage several printers that can be used by hundreds of clients: servers also store data files and handle email communications between clients. The client computers linked directly to a server constitute a *local area network (LAN)*. Within any organization there may be several LANs—for example, one in every division and function.

At the hub of a three-tier system are *mainframe computers*, large and powerful computers that can be used to store and process vast amounts of information. The mainframe can also be used to handle electronic communications between personal computers situated in different LANs. In addition, the mainframe may be connected to mainframes in other organizations and, through them, to LANs in other organizations. Increasingly, the Internet, a worldwide network of interlinked computers, is used as the conduit for connecting the computer systems of different organizations.

A manager with a personal computer hooked into a three-tier system can access data and software stored in the local server, in the mainframe, or through the Internet in computers based in another organization. A manager can therefore communicate electronically with other individuals hooked into the system, whether they are in the manager’s LAN, in another LAN within the manager’s organization, or in another organization altogether. Moreover, because of the growth of wireless communications, an individual with the proper equipment can hook into the system from any location—at home, on a boat, on the beach, in the air—anywhere a wireless communications link can be established.

Figure 13.4
A Typical Three-Tier Information System



Software developments

operating system

software Software that tells computer hardware how to run.

applications

software Software designed for a specific task or use.

artificial intelligence

Behavior performed by a machine that would be called intelligent if performed by a human being.

If computer hardware has been developing rapidly, so has computer software. **Operating system software** tells the computer hardware how to run. **Applications software**, such as programs for word processing, spreadsheets, graphics, and database management, is software developed for a specific task or use. The increase in the power of computer hardware has allowed software developers to write increasingly powerful programs that are, at the same time, increasingly user-friendly. By harnessing the rapidly growing power of microprocessors, applications software has vastly increased the ability of managers to acquire, organize, manipulate, and transmit information. In doing so, it also has increased the ability of managers to coordinate and control the activities of their organization and to make decisions, as discussed earlier.

Artificial intelligence is another interesting and potentially fruitful software development. **Artificial intelligence** has been defined as behavior by a machine that would be called intelligent if performed by a human being.⁵² Artificial intelligence has already made it possible to write programs that can solve problems and perform simple tasks. For example, software programs variously called “software agents,” “softbots,” or “knowbots” can be used to perform simple managerial tasks such as sorting through reams of data or incoming email messages to look for important data and messages. The interesting feature of these programs is that from “watching” a manager sort through such data they can “learn” what his or her preferences are. Having done this, they then can take over some of this work from the manager, freeing up more time for work on other tasks. Most of these programs are in the development stage, but they may be commonplace within a decade.⁵³



"Well, being single and a robot, I'm able to put in a lot of overtime."

Another software development that is starting to have an impact on the manager's job is speech recognition software. Currently speech recognition software must be "trained" to recognize and understand each individual's voice, and it requires the speaker to pause after each word. The increasing power of microprocessors, however, has enabled the development of faster speech recognition programs that can handle more variables and much greater complexity. Now a manager driving down the road may be able to communicate with a computer through a wireless link and give that computer complex voice instructions.⁵⁴

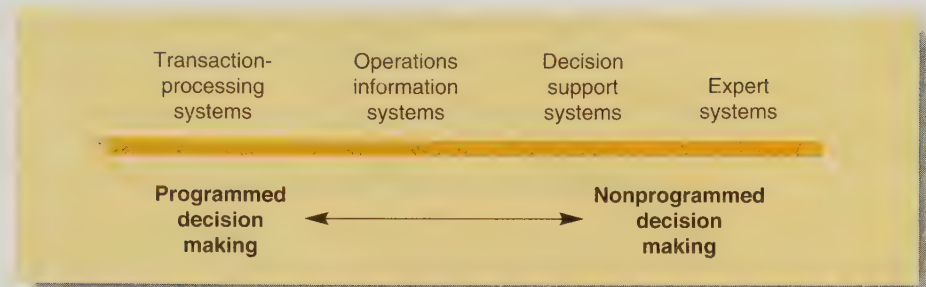
Types of Management Information Systems

Four types of computer-based management information systems can be particularly helpful in providing managers with the information they need to make decisions and to coordinate and control organizational resources: transaction-processing systems, operations information systems, decision support systems, and expert systems. In Figure 13.5, these systems are arranged along a continuum according to their increasing usefulness in providing managers with the information they need to make nonprogrammed decisions. (Recall from Chapter 5 that nonprogrammed decision making occurs in response to unusual, unpredictable opportunities and threats.) We examine each of these systems after focusing on the management information system that preceded them all: the organizational hierarchy.

The organizational hierarchy: The traditional information system

Traditionally, managers have used the organizational hierarchy as a system for gathering the information they need to achieve coordination and control and make decisions (see Chapter 7 for a discussion of organizational structure and hierarchy). According to business historian Alfred Chandler, the use of the hierarchy as an information network was perfected by railroad companies in the United States during the 1850s.⁵⁵ At that time, the railroads were the largest industrial organizations in the United States. By virtue of their size and geographical spread, they faced unique problems of coordination and control. In the 1850s, they started to solve these problems by designing hierarchical management structures that provided senior managers with the information they needed to achieve coordination and control and to make decisions about running the railroads.

Figure 13.5
Four Computer-
Based
Management
Information
Systems



Daniel McCallum, superintendent of the Erie Railroad in the 1850s, realized that the lines of authority and responsibility defining the Erie's management hierarchy also represented channels of communication along which information traveled. McCallum established what was perhaps the first modern management information system. Regular daily and monthly reports were fed up the management chain so that top managers could make decisions about, for example, controlling costs and setting freight rates. Decisions were then relayed back down the hierarchy so they could be carried out. Imitating the railroads, most other organizations used their hierarchies as systems for collecting and channeling information. This practice began to change only when electronic information technologies became more reasonably priced in the 1960s.

Although the organizational hierarchy is a useful information system, several drawbacks are associated with it. First, in organizations with many layers of managers, it can take a long time for information to travel up the hierarchy and for decisions to travel back down. This slow pace can reduce the timeliness and usefulness of information and prevent an organization from responding quickly to changing market conditions.⁵⁶ Second, information can be distorted as it moves from one layer of management to another. **Information distortion**, changes in meaning that occur as information passes through a series of senders and receivers, reduces the quality of information.⁵⁷ Third, because managers have only a limited span of control, as an organization grows larger, its hierarchy lengthens and this tall structure can make the hierarchy a very expensive information system. The popular idea that companies with tall management hierarchies are bureaucratic and unresponsive to the needs of their customers arises from the inability of tall hierarchies to effectively process data and provide managers with timely, complete, relevant, and high-quality information. Until modern computer-based information systems came along, however, the management hierarchy was the best information system available.

information distortion Changes in meaning that occur as information passes through a series of senders and receivers.

Transaction-processing systems

transaction-processing system A management information system designed to handle large volumes of routine, recurring transactions.

A **transaction-processing system** is a system designed to handle large volumes of routine, recurring transactions. Transaction-processing systems began to appear in the early 1960s with the advent of commercially available mainframe computers. They were the first type of computer-based management information system adopted by many organizations, and today they are commonplace. Bank managers use a transaction-processing system to record deposits into, and payments out of, bank accounts. Supermarket managers use a transaction-processing system to record the sale of items and to track inventory levels. More generally,

most managers in large organizations use a transaction-processing system to handle tasks such as payroll preparation and payment, customer billing, and payment of suppliers.

Operations information systems

operations information system

A management information system that gathers, organizes, and summarizes comprehensive data in a form that managers can use in their nonroutine coordinating, controlling, and decision-making tasks.

Many types of management information systems followed hard on the heels of transaction-processing systems in the 1960s. An **operations information system** is a system that gathers comprehensive data, organizes it, and summarizes it in a form that is of value to managers. Whereas a transaction-processing system processes routine transactions, an operations information system provides managers with information that they can use in their nonroutine coordinating, controlling, and decision-making tasks. Most operations information systems are coupled with a transaction-processing system. An operations information system typically accesses data gathered by a transaction-processing system, processes that data into useful information, and organizes that information into a form accessible to managers. Managers often use an operations information system to obtain sales, inventory, accounting, and other performance-related information. For example, the information that T. J. Rodgers at Cypress Semiconductor gets on individual employee goals and performance is provided by an operations information system.

Airborne Express uses an operations information system to track the performance of its 1,000 or so ground stations. Each ground station is evaluated according to four criteria: delivery (the goal is to deliver 95 percent of all packages by noon the day after they were picked up), productivity (measured by the number of packages shipped per employee-hour), controllable cost, and station profitability. Each ground station also has specific delivery, efficiency, cost, and profitability targets that it must attain. Every month Airborne's operations information system is used to gather information on these four criteria and summarize it for top managers, who are then able to compare the performance of each station against its previously established targets. The system quickly alerts senior managers to underperforming ground stations, so they can intervene selectively to help solve any problems that may have given rise to the poor performance.⁵⁸

Decision support systems

decision support system

An interactive computer-based management information system with model-building capability that managers can use when they must make nonroutine decisions.

A **decision support system** is an interactive computer-based system that provides models that help managers make better nonprogrammed decisions.⁵⁹ Recall from Chapter 5 that nonprogrammed decisions are decisions that are relatively unusual or novel, such as decisions to invest in new productive capacity, develop a new product, launch a new promotional campaign, enter a new market, or expand internationally. Although an operations information system organizes important information for managers, a decision support system gives managers a model-building capability and so provides them with the ability to manipulate information in a variety of ways. Managers might use a decision support system to help them decide whether to cut prices for a product. The decision support system might contain models of how customers and competitors would respond to a price cut. Managers could run these models and use the results as an *aid* to decision making.

The stress on the word *aid* is important, for in the final analysis a decision support system is not meant to make decisions for managers. Rather, its function is to provide valuable information that managers can use to improve the quality of their decision making. A good example of a sophisticated decision support system, developed by Judy Lewent, chief financial officer of the U.S. pharmaceutical company Merck, is given in the next “Manager as a Person.”

Manager as a Person

How Judy Lewent Became One of the Most Powerful Women in Corporate America

With annual sales of over \$45 billion, Merck is one of the largest developers and marketers of advanced pharmaceuticals. In 2000, the company spent more than \$3 billion on R&D to develop new drugs—an expensive and difficult process fraught with risk. Most new drug ideas fail to emerge from development. It takes an average of \$300 million and 10 years to bring a new drug to market, and 7 out of 10 new drugs fail to make a profit for the developing company.

Given the costs, risks, and uncertainties of new drug development, Judy Lewent, then director of capital analysis at Merck, decided to develop a decision support system that could help managers make more effective R&D investment decisions. Her aim was to give Merck’s top managers the information they needed to evaluate proposed R&D projects on a case-by-case basis. The system that Lewent and her staff developed is referred to in Merck as the “Research Planning Model.”⁶⁰ At the heart of this decision support system is a sophisticated model. The input variables include data on R&D spending, manufacturing costs, selling costs, and demand conditions. The relationships between the input variables are modeled by means of several equations that factor

in the probability of a drug’s making it through development and to market. The outputs of this modeling process are the revenues, cash flows, and profits that a project might generate.

The Merck model does not use a single value for an input variable, nor does it compute a single value for each output. Rather, a range is specified for each input variable (such as high, medium, and low R&D spending). The computer repeatedly samples at random from the range of values for each input variable and produces a probability distribution of values for each output. So, for example, instead of stating categorically that a proposed R&D project will yield a profit of \$500 million, the decision support system produces a probability distribution. It might state that although \$500 million is the most likely profit, there is a 25 percent chance that the profit will be



Judy Lewent, chief financial officer of Merck, consults with managers of Sweden’s Astra Pharmaceuticals as they work out the details of their global venture.

less than \$300 million and a 25 percent chance that it will be greater than \$700 million.

Merck now uses Lewent's decision support system to evaluate all proposed R&D investment decisions. In addition, Lewent has developed other decision support system models that Merck's managers can use to help them decide, for example, whether to enter into joint ventures with other companies or how best to hedge foreign exchange risk. As for Lewent, her reward was promotion to the position of chief financial officer of Merck. She is one of the most powerful women in corporate America.

Expert systems and artificial intelligence

expert system A management information system that employs human knowledge captured in a computer to solve problems that ordinarily require human expertise.

Expert systems are the most advanced management information systems available. An **expert system** is a system that employs human knowledge captured in a computer to solve problems that ordinarily require human expertise.⁶¹ Expert systems are a variant of artificial intelligence.⁶² Mimicking human expertise (and intelligence) requires a computer that can at a minimum (1) recognize, formulate, and solve a problem; (2) explain the solution; and (3) learn from experience.

Recent developments in artificial intelligence that go by names such as "fuzzy logic" and "neural networks" have resulted in computer programs that, in a primitive way, try to mimic human thought processes. Although artificial intelligence is still at a fairly early stage of development, an increasing number of business applications are beginning to emerge in the form of expert systems. General Electric, for example, has developed an expert system to help troubleshoot problems in the diesel locomotive engines it manufactures. The expert system was originally based on knowledge collected from David Smith, GE's top locomotive troubleshooter, who retired in the 1980s after 40 years of service at GE. A novice engineer or technician can use the system to uncover a fault by spending only a few minutes at a computer terminal. The system can explain to the user the logic of its advice, thereby serving as a teacher as well as a problem solver. The system is based on a flexible, humanlike thought process, and it can be updated to incorporate new knowledge as it becomes available. GE has installed the system in every railroad repair shop that it serves, thus eliminating delays and boosting maintenance productivity.⁶³

Limitations of Information Systems

Despite their usefulness, information systems have some limitations. A serious potential problem is the one noted at the beginning of this chapter. In all of the enthusiasm for management information systems, electronic communication by means of a computer network, and the like, a vital human element of communication may be lost. Some kinds of information cannot be aggregated and summarized on an MIS report because of issues surrounding information richness. Very rich information is often required to coordinate and control an

enterprise and to make informed decisions, far beyond that which can be quantified and aggregated.

The importance of information richness is a strong argument in favor of using electronic communication to *support* face-to-face communication, not to replace it. For example, it would be wrong to make a judgment about an individual's performance merely by "reading the numbers" provided by a management information system. Instead, the numbers should be used to alert managers to individuals who may have a performance problem. The nature of this performance problem should then be explored in a face-to-face meeting, during which rich information can be gathered. As a top Boeing manager noted, "In our company, the use of email and videoconferencing has not reduced the need to visit people at other sites; it has increased it. Email has facilitated the establishment of communications channels between people who previously would not communicate, which is good, but direct visits are still required to cement any working relationships that evolve out of these electronic meetings."

Summary and Review

INFORMATION AND THE MANAGER'S JOB

Computer-based information systems are central to the operation of most organizations. By providing managers with high-quality, timely, relevant, and relatively complete information, properly implemented information systems can improve managers' ability to coordinate and control the operations of an organization and to make effective decisions. Moreover, information systems can help the organization to attain a competitive advantage through their beneficial impact on productivity, quality, innovation, and responsiveness to customers.

COMMUNICATION AND MANAGEMENT Communication is the sharing of information between two or more individuals or groups to reach a common understanding. Good communication is necessary for an organization to gain a competitive advantage. Communication occurs in a cyclical process that entails two phases, transmission and feedback.

INFORMATION RICHNESS AND COMMUNICATION MEDIA

Information richness is the amount of information a communication medium can carry and the extent to which the medium enables the sender and receiver to reach a common understanding. Four categories of communication media in descending order of information richness are face-to-face communication (includes videoconferences), spoken communication electronically transmitted (includes voice mail), personally addressed written communication (includes email), and impersonal written communication (includes newsletters).

THE INFORMATION TECHNOLOGY REVOLUTION Over the last 30 years there have been rapid advances in the power, and rapid declines in the cost, of information technology. Falling prices, wireless communication, computer networks, and software developments have all radically improved the power and efficacy of computer-based information systems.

TYPES OF MANAGEMENT INFORMATION SYSTEMS Traditionally managers used the organizational hierarchy as the main system for gathering the information they needed to coordinate and control the organization and to make effective decisions. Today, managers use four types of computer-based information systems. Listed in ascending order of sophistication, they are transaction-processing systems, operations information systems, decision support systems, and expert systems.



Management in Action

Topics for Discussion and Action

1. What is the relationship between information systems and competitive advantage?
2. Which medium (or media) do you think would be appropriate for each of the following kinds of messages that a subordinate could receive from his or her boss: (a) a raise, (b) not receiving a promotion, (c) an error in a report prepared by the subordinate, (d) additional job responsibilities, and (e) the schedule for company holidays for the upcoming year? Explain your choices.
3. Ask a manager to describe the main kinds of information systems that he or she uses on a routine basis at work.
4. Because of the growth of high-powered low-cost computing, wireless communications, and technologies such as videoconferencing, many managers soon may not need to come into the office; they will be able to work at home. What are the pros and cons of such an arrangement?
5. Many companies have reported that it is difficult to implement advanced management information and decision support systems. Why do you think this is so? How might the roadblocks to implementation be removed?
6. Why is face-to-face communication between managers still important in an organization?



Building Management Skills

Diagnosing Ineffective Communication

Think about the last time you experienced very ineffective communication with another person—someone you work with, a classmate, a friend, a member of your family. Describe the incident. Then answer these questions.

1. Why was your communication ineffective in this incident?
2. What stages of the communication process were particularly problematic and why?
3. Describe any filtering or information distortion that occurred.
4. How could you have handled this situation differently so that communication would have been effective?



Small Group Breakout Exercise

Using New Information Systems

Form groups of three or four people, and appoint one member as the spokesperson who will communicate your findings to the whole class when called upon by the instructor. Then discuss the following scenario.

You are a team of managing partners of a large firm of accountants. You are responsible for auditing your firm's information systems to determine whether they are appropriate and up-to-date. To your

surprise, you find that although your organization does have an email system in place and accountants are connected into a powerful local area network (LAN), most of the accountants (including partners) are

not using this technology. You also find that the organizational hierarchy is still the preferred information system of the managing partners.

Given this situation, you are concerned that your organization is



not exploiting the opportunities offered by new information systems to obtain a competitive advantage. You have discussed this issue and are meeting to develop an action plan to get accountants to appreciate the need to learn, and to take advantage of, the potential of the new information technology.

1. What advantages can you tell accountants they will obtain when they use the new information technology?
2. What problems do you think you may encounter in convincing accountants to use the new information technology?
3. Discuss how you might make it easy for accountants to learn to use the new technology.



Be the Manager

Mark Chen supervises support staff for an Internet merchandising organization that sells furniture over the Internet. Chen has always thought that he should expand his staff. When he was about to approach his boss with such a request, the economy slowed, and other areas of the company experienced layoffs. Thus, Chen's plans for trying to add to his staff are on indefinite hold.

Chen has noticed a troubling pattern of communication with his staff. Ordinarily, when he wants one of his staff members to work on a task, he emails the pertinent infor-

mation to that person. For the last few months, his email requests have gone unheeded, and his subordinates comply with his requests only after he visits with them in person and gives them a specific deadline. Each time, they apologize for the delay but say that they are so overloaded with requests that they sometimes stop answering their phones. Unless someone asks for something more than once, they feel a request is not particularly urgent and can be put on hold.

Chen thinks this state of affairs is deplorable. He realizes, however, that his subordinates have no way

of prioritizing tasks and that is why some very important projects were put on hold until he inquired about them. Knowing that he cannot add to his staff in the short term, Chen has come to you for advice. He wants to develop a system whereby his staff will provide some kind of response to requests within 24 hours, will be able to prioritize tasks, identifying their relative importance, and will not feel so overloaded that they ignore their boss's requests and don't answer their phones. As an expert in communication, advise Chen.

A Problem in Communication



Additional Activities on the Build Your Management Skills DVD

- **Self-Assessment:**
(1) Active Listening Skills Inventory and (2) What Is Your Communication Style Under Stress?
- **Test Your Knowledge:**
(1) Choosing the Best Communication Medium, (2) Barriers to Effective Communications, and (3) Technological Change
- **Manager's Hot Seat:**
(1) Listening Skills: Yeah, Whatever and (2) Privacy: Burned by the Firewall?

Managing Ethically

In organizations today, employees often take advantage of their company's information systems. Email abuse is increasing, and so is the amount of time employees spend surfing the Internet on company time. Indeed, statistics suggest that approximately 70 percent of the total amount of time spent surfing the Internet is company time.

Questions

1. Either by yourself or in a group, explore the ethics of using IT for personal uses at work. Should employees have some rights to use these resources? When does their behavior become unethical?
2. Some companies keep track of the way their employees use IT and the Internet. Is it ethical for managers to read employees' private email or to record the sites that employees visit on the World Wide Web?



BusinessWeek

Case in the News

Blogging with the Boss's Blessing

Log on to Sara Ford's Web log, and you'll get a cinema verité look into her daily world. You'll learn about her addiction to TV shows starring Richard Dean Anderson (aka MacGyver), her geek penchant for jokes with punchlines like "F1 F1!", and why she adores Gore-Tex. But most important, you'll learn that 26-year-old Sara Ford is a software design engineer at Microsoft Corp., blogging away from her fluorescent-lit office in Redmond, Wash. Her most prominent posts are ones about the product she's working on, its latest bugs, and inside dope for users such as the "hide underline letters checkbox issue." There's also her day-in-the-life workplace diary, complete with a glossary decoding Microsoft arcana and strategies for nabbing extra espresso coupons. Customers post replies. Ideas are swapped. Bonds are formed. And Bill Gates is happy.

Until recently, the thought of employees blabbing freely to the masses about their work on company time—without the suits from

PR hovering over them to stay "on message"—would have created panic in the executive suite. But in the past year, employee blogs have begun to multiply across Corporate America—and a growing number of companies approve. It started mostly as a techie thing when engineers and product developers at places such as Macromedia, Sun Microsystems, and Dell began posting first-draft free-for-alls of their own volition as a way of communicating with customers, each other, and the outside world. Though employees represent just a fraction of the 2.7 million bloggers today, experts predict they will grow robustly as consumers demand information in a more unvarnished way.

Increasingly, execs see employee blogs as a way to transform a transaction with a faceless behemoth into a personal relationship with an employee. Blogs are also hyper efficient at driving product innovation. And they create loyal audiences. Once people get hooked, they keep coming back for more. "This is nothing less than revolu-

tionary," says Dave Winer, a fellow at Harvard Law School's Berkman Center for Internet & Society.

It's revolutionary because companies have usually been more concerned with controlling their message than conversing with customers. Blogging changes that by establishing "a connection through real human beings speaking like real human beings, which is something companies have forgotten how to do," says David Weinberger, the Boston-based co-author of *The Cluetrain Manifesto*.

Microsoft has been one of the biggest evangelists. A year ago, it had about 100 corporate bloggers. Today there are 800. They post pictures of company refrigerators—there's one that has all Coke and one that has all Pepsi—and spout off on everything from the death of Boots the cat to renaming Longhorn, Microsoft's long-anticipated new operating system, "Longwait." Indeed, Chairman William H. Gates III is so certain that corporate blogging is the next gold rush in communications that he's practically

handing out the pails and shovels by enabling any employee to create a blog within two seconds. Microsoft doesn't train employees in the fine art of blogs, but employees hold meetings to talk about them. The blogs carry disclaimers, but other than that, "our outspoken policy on blogging is: Don't be stupid," says product manager Adam Sohn.

Going Further

Other companies, such as publisher Ziff-Davis, started the process by setting up internal blogs that proved enormously helpful to teams by cutting down on email. They also let employees learn what was appropriate when blogging to the outside. Nike is going further. This month the company launched a blog of its own—"The Art of Speed"—and hired hip gossip blogger extraordinaire, Gawker Media, to produce it. Nike says Gawker has the following it wants to reach.

Given blogging's ability to give nobodies such awesome powers—*The New York Post* headlined the

way political bloggers did in former Senate Majority Leader Trent Lott as "The Internet's First Scalp"—you'd think the idea of workers firing off would strike companies as akin to putting dynamite in the playpen. This is, after all, a medium once referred to as the electronic Jerry Springer.

Indeed, blogs can be dangerous, representing a new legal netherworld. Microsoft's most famous blogger, Robert "Scobleizer" Scoble once got into big trouble in a previous job for talking up a rival's products. Therein lies the rub: The most truthful they are, the more valuable blogs are to customers. It's likely only a matter of time before some workplace pundit spills a trade secret, unwittingly leaks a clandestine launch date, or takes a swipe at a CEO that turns into slander.

For now, though, many are running the risk. In an era of fragmental media, with companies struggling to get their message out any which way, blogs are becoming a kind of undercover megaphone. One way to think of them is as the latest guer-

rilla marketing tool, a new kind of brand bait.

They'll likely backfire, though, if employers attempt to exert control. "Companies inevitably will try to co-opt blogs," says Dan Gillmore, author of *We, the Media*, a book about blogging due out next month.

Until then, happy reading.

Questions

1. What are the potential advantages of blogging at work by employees in high-tech companies?
2. What are the potential disadvantages?
3. For what other kinds of companies might blogging be potentially advantageous?
4. Are there organizations in which blogging should be prohibited? Why or why not?

Source: M. Conlin and A. Park, "Blogging with the Boss's Blessing." Reprinted from the June 28, 2004, issue of *BusinessWeek* by special permission. Copyright © 2004 by the McGraw-Hill Companies, Inc.

Last year, the revival that lifted the rest of the online industry left America Online Inc. in the dust. Even as a rebound in ads sent 2003 profits at rival Yahoo! Inc. spiking 123 percent, AOL's subscribers jumped ship in droves for low-cost dial-up competitors or broadband providers. Ad revenue sank 40 percent, to \$787 million, and federal investigators continued to probe AOL's past ad deals for accounting irregularities. As operating earnings before depreciation and amortiza-

tion fell 2 percent, to \$1.5 billion, Wall Street started betting that Time Warner Inc. would ditch AOL the first change it got.

But AOL's date with the dump has been postponed, if not canceled. On June 24, Time Warner paid \$435 million in cash to buy Advertising.com Inc., a leading online-ad-placement company that should help boost AOL's ad revenue. "Our emphasis is on building up the AOL business," says Time Warner CEO Richard D. Parsons.

Chalk up one for AOL CEO Jonathan F. Miller. After struggling to regain focus after its rocky 2001 merger with Time Warner, AOL is finding its footing again with Miller's new strategy: providing a menu of online services ranging from full-blown broadband service to à la carte online music subscriptions to cheap, no-frills dial-up access. "We'd gotten behind in the market," he says. "We're putting in a business model appropriate to where the world is going."

Miller hasn't yet proven that the world will order from his menu, but a rebound in AOL's advertising and global businesses will buy him time. Combined with cost cuts, that should produce the double-digit profit growth this year that Time Warner expects, says Richard Greenfield, media analyst at Fulcrum Global Partners LLC. Still, the heart of Miller's strategy—persuading customers who have signed up with another broadband provider to also buy AOL's broadband services—is a gamble. "They haven't turned the battleship around yet," says David Card, online-media analyst at Jupiter Research.

In the new world, Miller is counting on profit gains, not revenue growth, to float AOL's boat. The company's old \$23.90-a-month dial-up service made for fat revenues but slimmer profits, thanks to the cost of providing network connections. New, lower-priced broadband services will produce less revenue but higher margins since AOL won't have to pay network access fees. It expects earnings from ads, broadband and premium services, and global sales to rise 30 percent to 50 percent annually over the next few years.

Not Just Eyeballs

An ad revival is starting to help. For the first time since 2001, ad revenue should rise 11 percent in 2004, to \$873 million, says Deutsche Bank (DB). Advertising.com should send them up even more. It specializes in a new results-driven approach: charging advertisers for the number of online transactions generated by ads, not just the number of eyeballs reached.

Meanwhile, Miller is stanching the bleeding from AOL's dwindling dial-up base. To preserve margins, AOL is renegotiating contracts with network providers such as MCI Inc. As dial-up members leave, AOL can cut network costs associated with them.

That leaves Miller freer to pursue his "superstore on the Web" strategy. To match low-cost rivals, there's a new \$9.95-a-month dial-up Netscape Communications service. For members considering a move to broadband rivals, there's a \$14.95-a-month AOL for Broadband service. How will he persuade consumers to buy AOL's package of content and services if they use someone else's pipe to get online?

By offering bite-size premium services such as \$8.95-a-month online music subscriptions. And AOL is offering free samples of content from Time Warner's video-on-demand and Road Runner broadband units. The plan shows signs of working. In the first quarter, 600,000 people signed up for the broadband services, for a total of 3.5 million.

AOL remains a long way from a sustained revival. But with healthier ad sales, slimmer costs, and a rosier global outlook, Miller—and Time Warner—can afford to throw the dice for now.

Questions

1. What are Miller's new strategies for AOL?
2. How is he changing AOL to achieve them?

Source: Catherine Yang, Tom Lowry, and Ben Elgin, "America Online Gets Clicking." Reprinted from the July 12, 2004, issue of *BusinessWeek* by special permission. Copyright © 2004 by the McGraw-Hill Companies, Inc.

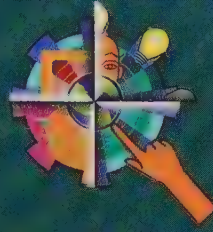
CHAPTER 14

Operations Management: Managing Vital Operations and Processes

Learning Objectives

After studying this chapter, you should be able to:

- Explain the role of operations management in achieving superior quality, efficiency, and responsiveness to customers.
- Describe what customers want, and explain why it is so important for managers to be responsive to their needs.
- Explain why achieving superior quality in an organization's operations and processes is so important.
- Explain why achieving superior efficiency is so important.
- Differentiate among facilities layout, flexible manufacturing, just-in-time inventory, and process reengineering.



Management Snapshot

Why Toyota Is a Leader in Operations Management

How can managers work to increase operating performance?

Toyota has long been known as a company that constantly works to modify and change its production systems to improve efficiency, quality, and customer responsiveness. Toyota pioneered the system of lean production, the continuous incremental improvement of work procedures that results in dramatic improvements in vehicle quality. In lean production, employees become responsible for improving work procedures to drive down costs and drive up quality. Individually, and in quality groups or circles, employees suggest ways to improve how a particular Toyota car model is made. Over time, their thousands of suggestions result in major improvements to the final product. Employees receive cash bonuses and rewards for finding ways to improve work procedures, and the result has been a continuous increase in car quality and reduced manufacturing costs.

In the early 2000s, under the leadership of its then president, Jujio Cho, Toyota strived to increase further its efficiency and quality.

Toyota wanted to maintain competitive advantage over global competitors such as General Motors, Ford, and DaimlerChrysler, car companies that also utilized lean production. So, Toyota began a series of programs with the goal of improving selected aspects of its operations.



Assembly line workers for Japanese auto giant Toyota put tires onto Toyota's vehicle "V" at the company's Tsutsumi plant in Toyota, central Japan. Toyota is widely credited with pioneering a number of critical innovations in the way cars are built that have helped it achieve superior productivity and quality—the basis of Toyota's competitive advantage.

One of the programs called "pokayoke" or mistake-proofing concentrates on the stages of the assembly process that previously have led to the most quality problems; employees

are required to double- and triple-check a particular stage to discover any defective parts or to fix improper assembly operations that may lead to subsequent customer complaints. Another program is CCC21, in which Toyota is working continually with its suppliers to find ways to reduce the costs of the cars' components. By 2005, these costs were reduced by 30 percent and Toyota saved billions of dollars a year in operating costs.

Another change Toyota made introduced a new manufacturing process called GBL, which uses a sophisticated new assembly process to hold a car body firmly in place during production so that all welding and assembly operations can be performed more accurately—and also resulting in a better quality vehicle. GBL

has also allowed Toyota to build factories that can assemble several different kinds of cars along the same production line with no loss in efficiency or quality. This initiative is a major source of competitive advantage because Toyota's global network of car plants can now move quickly to alter the cars they are making to respond to increasing or decreasing customer demand for a certain type of vehicle.

Toyota's mastery of production operations and processes has made it by far the most profitable global carmaker. With all its new operations initiatives proceeding at full speed, Toyota replaced Ford as the world's second largest carmaker in 2004 and has set its sights on replacing GM as the world's biggest carmaker by 2010.

Overview

operations management The management of any aspect of the production system that transforms inputs into finished goods and services.

Toyota constantly searches for ways to improve its vehicle assembly operations and processes to reduce costs and improve quality, allowing the company to be more responsive to customers who purchase a high-quality vehicle for a reasonable price. (An interesting article at the end of this chapter describes how Toyota began production in China to drive down costs.)

In this chapter we focus on operations management techniques that managers can use to increase the quality of an organization's products, the efficiency of production, and the organization's responsiveness to customers. By the end of this chapter, you will understand the vital role operations management plays in building competitive advantage and creating a high-performing organization.

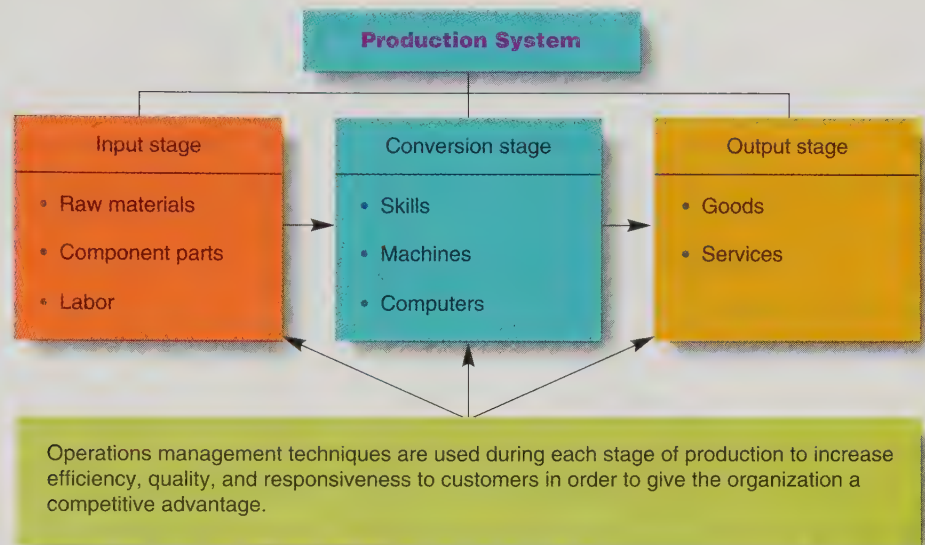
Operations Management and Competitive Advantage

production system The system that an organization uses to acquire inputs, convert the inputs into outputs, and dispose of the outputs.

Operations management is the management of any aspect of the production system that transforms inputs into finished goods and services. A **production system** is the system that an organization uses to acquire inputs, convert inputs into outputs, and dispose of the outputs (goods or services). **Operations managers** are managers who are responsible for managing an organization's production system. They do whatever it takes to transform inputs into outputs. Their job is to manage the three stages of production—acquisition of inputs, control of conversion processes, and disposal of goods and services—and to determine where operating improvements might be made in order to increase quality, efficiency, and responsiveness to customers and so give an organization a competitive advantage (see Figure 14.1).

Quality refers to goods and services that are reliable, dependable, or psychologically satisfying: They do the job they were designed for and do it well, or they possess some attribute that gives their users something they value.¹ *Efficiency* refers to the amount of inputs required to produce a given output. *Responsiveness to customers* refers to actions taken to meet the demands and needs of customers. Operations

Figure 14.1
The Purpose
of Operations
Management



operations manager A manager who is responsible for managing an organization's production system and for determining where operating improvements might be made.

managers are responsible for ensuring that an organization has sufficient supplies of high-quality, low-cost inputs, and they are responsible for designing a production system that creates high-quality, low-cost products that customers are willing to buy. The "Management Insight" on page 493 describes how Citibank used new IT to improve its responsiveness to customers.

Notice that achieving superior efficiency and quality is part of attaining superior responsiveness to customers. Customers want value for their money, and an organization whose efficient production system creates high-quality, low-cost products is best able to deliver this value. For this reason, we begin by discussing how operations managers can design the production system to increase responsiveness to customers.

Improving Responsiveness to Customers

Organizations produce outputs—goods or services—that are consumed by customers. All organizations, profit seeking or not-for-profit, have customers. Without customers, most organizations would cease to exist. Because customers are vital to the survival of most organizations, managers must correctly identify customers and promote organizational strategies that respond to their needs. This is why management writers recommend that organizations define their business in terms of the customer needs they are satisfying, not the type of products they are producing.² The credo of pharmaceutical company Johnson & Johnson, for example, begins, "We believe our first responsibility is to the doctors, nurses and patients, to mothers and fathers and all others who use our products and services."³ Through the credo Johnson & Johnson's managers emphasize their commitment to exemplary customer service. In contrast, in the early 2000s, Lucent Technologies decided that, given its expertise in transistor technology, it would focus on producing transistor-based Internet routers that could handle vast quantities of information. When it became clear that customers were choosing optical Internet routers because these routers could transfer information extremely quickly, Lucent lost a large part of its business.

What do customers want?

Given that satisfying customer demands is central to the survival of an organization, an important question is, What do customers want? To specify exactly what they want is not possible because their wants vary from industry to industry. However, it is possible to identify some universal product attributes that most customers in most industries want. Generally, other things being equal, most customers prefer

1. A lower price to a higher price
2. High-quality products to low-quality products
3. Quick service to slow service (They will always prefer good after-sales service and support to poor after-sales support.)
4. Products with many features to products with few features (They will prefer a personal computer with a CD-ROM drive, lots of memory, and a powerful micro-processor to one without these features.)
5. Products that are, as far as possible, customized or tailored to their unique needs

Of course, the problem is that other things are not equal. For example, providing high quality, quick service, and after-sales service and support, products with many features, and products that are customized raises costs and thus the price that must be charged to cover costs.⁴ So customers' demands for these attributes typically conflict with their demands for low prices. Accordingly, customers must make a trade-off between price and preferred attributes, and so must managers.

Designing production systems to be responsive to customers

Because satisfying customers is so important, managers try to design production systems that can produce the outputs that have the attributes customers desire. The



A Southwest ticket agent assists a customer. Southwest's operating system is geared toward satisfying customer demands for low-priced, reliable, and convenient air travel, making it one of the most consistently successful airlines in recent years. To help keep flights on schedule, Southwest's workforce has been cross-trained to perform multiple tasks. For example, the person who checks tickets might also help with baggage loading.

attributes of an organization's outputs—their quality, cost, and features—are determined by the organization's production system.⁵ Since the ability of an organization to satisfy the demands of its customers derives from its production system, managers need to devote considerable attention to constantly improving production systems. Managers' desire to attract customers with improved products explains their adoption of many new operations management techniques in recent years. These include flexible manufacturing systems, just-in-time inventory, and, of course, the new information systems and technologies discussed in Chapter 13.

As an example of the link between responsiveness to customers and an organization's production system, consider the success of Southwest Airlines. One of the most consistently successful airlines in the United States, Southwest Airlines has been expanding rapidly. One reason for Southwest's success is that its managers created a production system

uniquely tailored to satisfy the demands of its customers for low-priced, reliable (on-time), and convenient air travel. Southwest commands high customer loyalty precisely because its production system delivers products, such as flights from Houston to Dallas, that have all the desired attributes: reliability, convenience, and low price.

Southwest's low-cost production system focuses not only on improving the maintenance of aircraft but also on the company's ticket reservation system, route structure, flight frequency, baggage-handling system, and in-flight services. Each of these elements of Southwest's production system is geared toward satisfying customer demands for low-priced, reliable, and convenient air travel. For example, Southwest offers a no-frills approach to in-flight customer service. No meals are served on board, and there are no first-class seats. Southwest does not subscribe to the big reservation computers used by travel agents because the booking fees are too costly. Also, the airline flies only one aircraft, the fuel-efficient Boeing 737, which keeps training and maintenance costs down. All this translates into low prices for customers.

Southwest's reliability derives from the fact that it has the quickest aircraft turnaround time in the industry. A Southwest ground crew needs only 15 minutes to turn around an incoming aircraft and prepare it for departure. This speedy operation helps to keep flights on time. Southwest has such quick turnaround because it has a flexible workforce that has been cross-trained to perform multiple tasks. Thus, the person who checks tickets might also help with baggage loading if time is short.

Southwest's convenience comes from its scheduling multiple flights every day between its popular locations, such as Dallas and Houston, and its use of airports that are close to downtown (Hobby at Houston and Love Field at Dallas) instead of more distant major airports.⁶ Another example of how a company used IT to increase responsiveness to customers is discussed in the following "Management Insight."



Management Insight

Citibank Uses CRM to Increase Customer Loyalty

Citibank, one of the leading global financial institutions, has established a goal of becoming the premier institution in the 21st century. To achieve this lofty goal, Citibank has started to use customer relationship management (CRM), an operations management technique, to increase its responsiveness to customers, recognizing that, ultimately, its customer base and customer loyalty determine the bank's future success.

As the first step in its CRM effort, Citibank identified the factors that dissatisfy its customers. When analyzing complaints, it found that most concerned the time it took to complete a customer's request, such as responding to an account problem or getting a loan. So Citibank managers began to examine how they handled each kind of customer request. For each distinct request, they formed a cross-functional team that broke down a specific request into the steps between people and departments that were needed to complete the request. In analyzing them, teams found that often many steps in the process were unnecessary and could be replaced by using the right information systems. They also found that delays often occurred because employees simply did not know how to handle a request. They were not being given the right kind of training, and when they couldn't handle a request, employees simply put it aside until a supervisor could deal with it.

Citibank's second step to increase responsiveness was to implement an organizationwide CRM program. Managers and supervisors were charged with reducing the complexity of the work process and finding the most effective way to process each particular request, such as a request for a loan. Managers were also charged with training employees to answer each specific request.

The results were remarkable. For example, in the loan department the CRM program reduced by 75 percent the number of handoffs necessary to process a request: The department's average response time dropped from several hours to 30 minutes. By 2000, more than 92,000 employees worldwide had been trained in the new CRM processes, and Citibank could easily measure CRM's effectiveness by the increased speed with which it was handling an increased volume of customer requests.

Although managers must seek to improve their responsiveness to customers by improving their organizations' production systems, they should not offer a level of responsiveness to customers that is more than that production system can profitably sustain. The company that customizes every product to the unique demands of individual customers is likely to see its cost structure become so high that unit costs exceed unit revenues. This happened to Toyota in the 1990s when Toyota managers' drive to provide customers with many choices of car models and specifications increased costs faster than it generated additional revenues. At one point, literally thousands of variations of Toyota's basic models, such as the Camry and Corolla, were being produced by Toyota factories. Managers at Toyota concluded that the costs of extreme customization were exceeding the benefits and cut back on the number of models and specifications of its cars.⁷

Improving Quality

As noted earlier, high-quality products are reliable, dependable, and satisfying; they do the job they were designed for and meet customer requirements.⁸ Quality is a concept that can be applied to the products of both manufacturing and service organizations—goods such as a Toyota car or a Kroger steak or services such as Southwest Airlines flight service or customer service in a Citibank branch. Why do managers seek to control and improve the quality of their organization's products?⁹ There are two reasons (see Figure 14.2).

First, customers usually prefer a higher-quality product to a lower-quality product. So an organization able to provide, *for the same price*, a product of higher quality

Figure 14.2
The Impact of Increased Quality on Organizational Performance



than a competitor's product is serving its customers better—it is being more responsive to its customers. Often, providing high-quality products creates a brand-name reputation for an organization's products. In turn, this enhanced reputation may allow the organization to charge more for its products than its competitors are able to charge and thus make even greater profits. In 2005, Lexus, Toyota's luxury car division, was number one on the J. D. Power list of the 10 most reliable car manufacturers and Toyota was the number four luxury car maker.¹⁰ The high quality of Toyota/Lexus vehicles has enabled the company to charge higher prices for its cars than the prices charged by rival automakers.

The second reason for trying to boost product quality is that higher product quality can increase efficiency and thereby lower operating costs and boost profits. Achieving high product quality lowers operating costs because of the effect of quality on employee productivity: Higher product quality means less employee time is wasted in making defective products that must be discarded or in providing substandard services, and less time has to be spent fixing mistakes. This translates into higher employee productivity, which means lower costs.

To increase quality, managers need to develop strategic plans that state goals exactly and spell out how they will be achieved. Managers should embrace the philosophy that mistakes, defects, and poor-quality materials are not acceptable and should be eliminated. First-line managers should spend more time working with nonmanagerial employees and providing them with the tools they need to do the job. Managers should create an environment in which subordinates will not be afraid to report problems or recommend improvements. Output goals and targets need to include not only numbers or quotas but also some notion of quality to promote the production of defect-free output. Managers also need to train employees in new skills to keep pace with changes in the workplace. Finally, achieving better quality requires managers to develop organizational values and norms centered on improving quality.

Improving Efficiency

The third goal of operations management is to increase the efficiency of an organization's production system. The fewer the inputs required to produce a given output, the higher will be the efficiency of the production system.

Managers can measure efficiency at the organization level in two ways. The measure known as *total factor productivity* looks at how well an organization utilizes all of its resources—such as labor, capital, materials, or energy—to produce its outputs. It is expressed in the following equation:

$$\text{Total factor productivity} = \frac{\text{outputs}}{\text{all inputs}}$$

The problem with total factor productivity is that each input is typically measured in different units: Labor's contribution to producing an output is measured by hours worked; the contribution of materials is measured by the amount consumed (for example, tons of iron ore required to make a ton of steel); the contribution of energy is measured by the units of energy consumed (for example, kilowatt-hours); and so on. To compute total factor productivity, managers must convert all the inputs to a common unit, such as dollars, before they can work the equation.

Though sometimes a useful measure of efficiency overall, total factor productivity obscures the exact contribution of an individual input—such as labor—to the production of a given output. Consequently, most organizations focus on specific measures of efficiency, known as *partial productivity*, that measure the efficiency of an individual unit. For example, the efficiency of labor inputs is expressed as

$$\text{Labor productivity} = \frac{\text{outputs}}{\text{direct labor}}$$

Labor productivity is most commonly used to draw efficiency comparisons between different organizations. For example, one study found that in 1994 it took the average Japanese automobile components supplier half as many labor hours to produce a part, such as a car seat or exhaust system, as the average British company.¹¹ Thus, the study concluded, Japanese companies use labor more efficiently than British companies.

The management of efficiency is an extremely important issue in most organizations, because increased efficiency lowers production costs, thereby allowing the organization to make a greater profit or to attract more customers by lowering its price. For example, in 1990 the price of the average personal computer sold in the United States was \$3,000, by 1995 the price was around \$1,800, and in 2001 it was \$750. This decrease occurred despite the fact that the power and capabilities of the average personal computer increased dramatically during this time period (microprocessors became more powerful, memory increased, modems were built in, and multimedia capability was added).

Why was the decrease in price possible? Manufacturers of personal computers such as Compaq and Dell focused on quality and boosted their efficiency by improving the quality of their components and making PCs easier to assemble. This allowed them to lower their costs and prices yet still make a profit.¹²

Facilities layout, flexible manufacturing, and efficiency

Another factor that influences efficiency is the way managers decide to lay out or design an organization's physical work facilities. This is important for two reasons. First, the way in which machines and workers are organized or grouped together into workstations affects the efficiency of the production system. Second, a major determinant of efficiency is the cost associated with setting up the equipment needed to make a particular product. **Facilities layout** is the operations management technique whose goal is to design the machine-worker interface to increase production system efficiency. **Flexible manufacturing** is the set of operations management techniques that attempt to reduce the setup costs associated with a production system.

FACILITIES LAYOUT The way in which machines, robots, and people are grouped together affects how productive they can be. Figure 14.3 shows three basic ways of arranging workstations: product layout, process layout, and fixed-position layout.

In a *product layout*, machines are organized so that each operation needed to manufacture a product is performed at workstations arranged in a fixed sequence.

facilities layout

The operations management technique whose goal is to design the machine-worker interface to increase production system efficiency.

flexible manufacturing

Operations management techniques that attempt to reduce the setup costs associated with a production system.

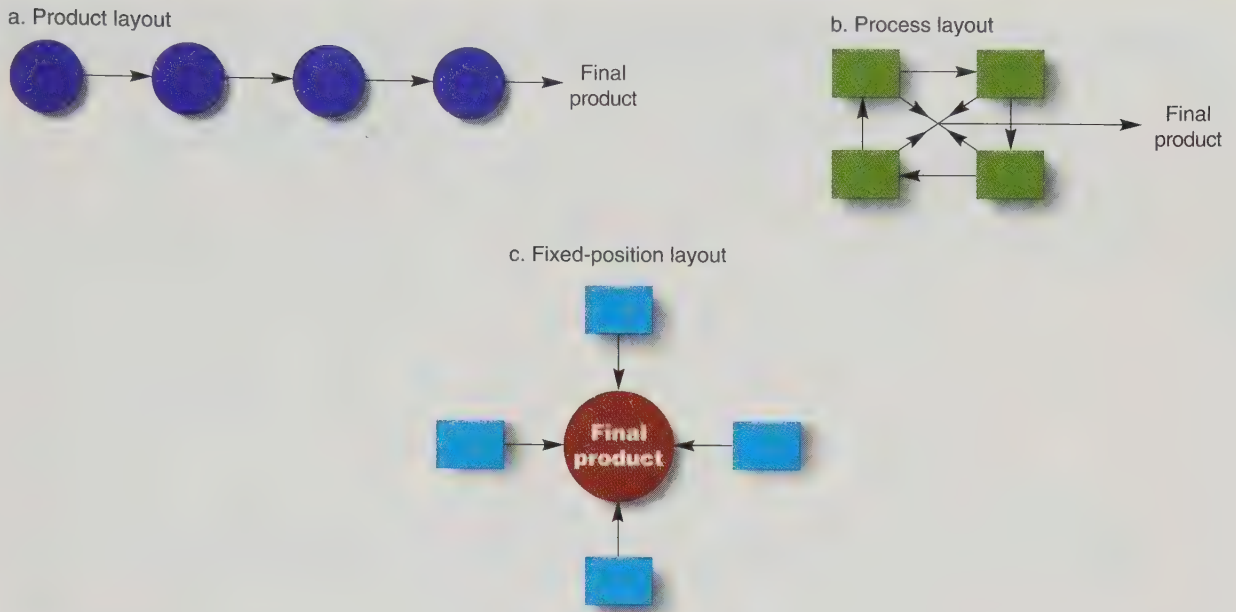


Figure 14.3
Three Facilities Layouts

Typically, workers are stationary in this arrangement, and a moving conveyor belt takes the product being worked on to the next workstation so that it is progressively assembled. Mass production is the familiar name for this layout; car assembly lines are probably the best-known example. Formerly product layout was efficient only when products were created in large quantities; however, the introduction of modular assembly lines controlled by computers makes it efficient to make products in small batches.

In a *process layout*, workstations are not organized in a fixed sequence. Rather, each workstation is relatively self-contained, and a product goes to whichever workstation is needed to perform the next operation to complete the product. Process layout is often suited to manufacturing settings that produce a variety of custom-made products, each tailored to the needs of a different kind of customer. For example, a custom furniture manufacturer might use a process layout so that different teams of workers can produce different styles of chairs or tables made from different kinds of woods and finishes. A process layout provides the flexibility needed to change the product. Such flexibility, however, often reduces efficiency because it is expensive.

In a *fixed-position layout*, the product stays in a fixed position. Its component parts are produced in remote workstations and brought to the production area for final assembly. Increasingly, self-managed teams are using fixed-position layouts. Different teams assemble each component part and then send these parts to the final assembly team, which makes the final product. A fixed-position layout is commonly used for products such as jet airlines, mainframe computers, and gas turbines—products that are complex and difficult to assemble or so large that moving them from one workstation to another would be difficult. The effects of moving

from one facilities layout to another can be dramatic, as the following “Manager as a Person” suggests.



Manager as a Person

How to Improve Facilities Layout

Paddy Hopkirk established his car accessories business in Bedfordshire, England, shortly after he had shot to motor car racing fame by winning the Monte Carlo Rally. Sales of Hopkirk's accessories, such as bicycle racks and axle stands, were always brisk, but Hopkirk was the first to admit that his production system left a lot to be desired, so he invited consultants to help reorganize his production system.

After analyzing his factory's production system, the consultants realized that the source of the problem was the facilities layout Hopkirk had established. Over time, as sales grew, Hopkirk simply added new workstations to the production system as they were needed. The result was a process layout in which the product being assembled moved in the irregular sequences shown in the “Before Change” half of Figure 14.4. The consultants suggested that to save time and effort, the workstations should be reorganized into the sequential product layout shown in the “After Change” illustration.

Once this change was made, the results were dramatic. One morning the factory was an untidy sprawl of workstations surrounded by piles of crates holding semifinished components. Two days later, when the 170-person workforce came back to work, the machines had been brought together into tightly grouped workstations arranged in the fixed sequence shown in the illustration. The piles of components had disappeared, and the newly cleared floor space was neatly marked with color-coded lines mapping out the new flow of materials between workstations.

In the first full day of production, efficiency increased by as much as 30 percent. The space needed for some operations had been cut in half, and work-in-progress had been cut considerably. Moreover, the improved layout allowed for some jobs to be combined, freeing operators for deployment elsewhere in the factory. An amazed Hopkirk exclaimed, “I was expecting a change but nothing as dramatic as this . . . it is fantastic.”¹³

FLEXIBLE MANUFACTURING In a manufacturing company, a major source of costs is the costs associated with setting up the equipment needed to make a particular product. One of these costs is the cost of production that is forgone because nothing is produced while the equipment is being set up. For example, components manufacturers often need as much as half a day to set up automated production equipment when switching from production of one component part (such as a washer ring for the steering column of a car) to another (such as a washer ring for the steering column of a truck). During this half-day, a manufacturing plant is not producing anything, but employees are paid for this “non-productive” time.

It follows that if setup times for complex production equipment can be reduced, so can setup costs, and efficiency will rise. In other words, if setup times can be

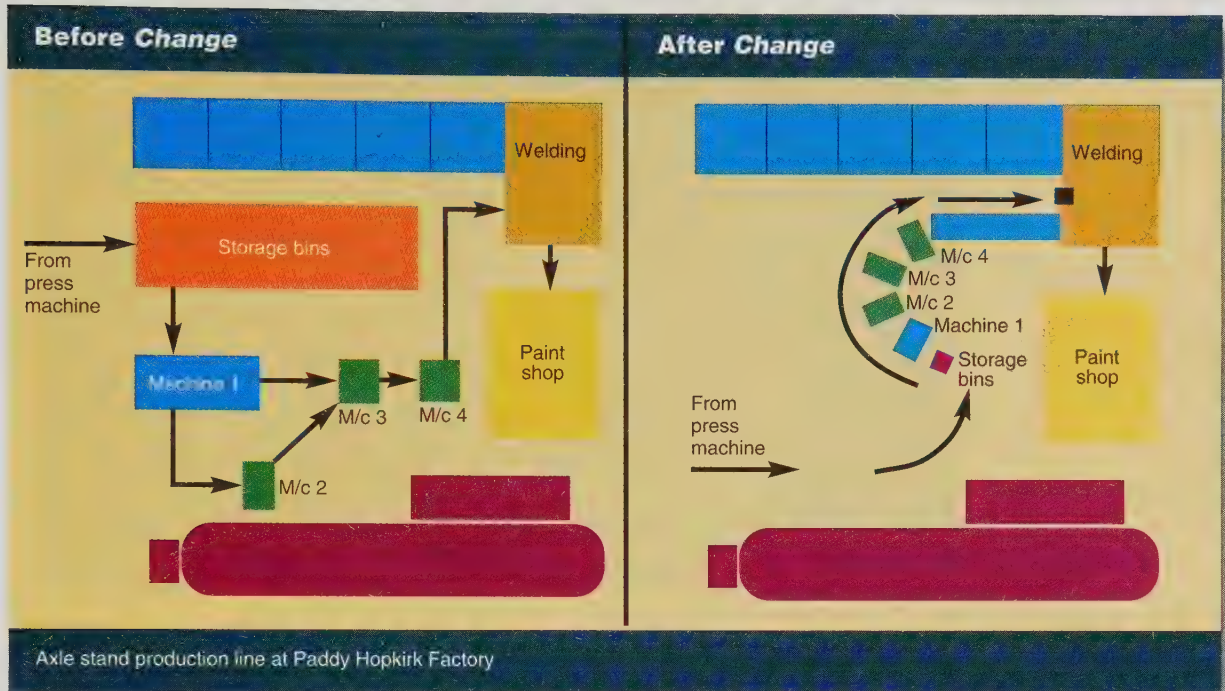


Figure 14.4
Changing a Facilities Layout

Source: Reprinted from *Financial Times* of January 4, 1994, by permission of Financial Times Syndication, London.

reduced, the time that plant and employees spend in actually producing something will increase. This simple insight has been the driving force behind the development of flexible manufacturing techniques.

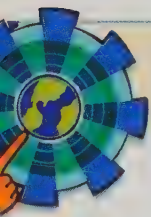
Flexible manufacturing aims to reduce the time required to set up production equipment.¹⁴ Redesigning the manufacturing process so that production equipment geared for manufacturing one product can be quickly replaced with equipment geared to make another product can dramatically reduce setup times and costs. Another favorable outcome from flexible manufacturing is that a company is able to produce many more varieties of a product than before in the same amount of time. Thus, flexible manufacturing increases a company's ability to be responsive to its customers.

Increasingly, organizations are experimenting with new designs for production systems that not only allow workers to be more productive but also make the work process more flexible, thus reducing setup costs. Some Japanese companies are experimenting with facilities layouts arranged as a spiral, as the letter Y, and as the number 6, to see how these various configurations affect setup costs and worker productivity. At a camcorder plant in Kohda, Japan, for example, Sony changed from a fixed-position layout in which 50 workers sequentially built a camcorder to a flexible spiral process design in which four workers perform all the operations necessary to produce the camcorder. This new layout allows the most efficient workers to work at the highest pace, and it reduces setup

Assisted by Web-based on-line work instructions, an operator at Dell Computer determines the sequence in which Dell's custom-built computers are to be assembled by its computer-controlled flexible manufacturing system. This flexible system makes possible Dell's low-cost strategy.



costs because workers can easily switch from one model to another, increasing efficiency by 10 percent.¹⁵ An interesting example of a company that built a new factory to obtain the benefits of flexible manufacturing is profiled in the following “Managing Globally.”



Managing Globally

Igus's Factory of the Future

Igus Inc., headquartered in Cologne, Germany, makes over 28,000 polymer bearings and energy supply cable products used in applications the world over. In the 1990s, the company's managers realized they needed to build a new factory that could handle the company's rapidly growing product line.¹⁶

Igus's product line changes constantly as new products are developed and old ones become obsolete. At Igus new products are often introduced on a daily basis, so the need for flexibility is great. Moreover, because many of its products are highly customized, the specific and changing needs of customers drive new product development.

Igus's new factory—as big as three football fields—was designed with the need for flexibility in mind. Nothing in the factory is tied down or bolted to the floor. All the machines, computers, and equipment can be moved and repositioned to suit changing product requirements. Moreover, all Igus employees are trained to be flexible and can perform many different production tasks. For example, when one new product line proved popular with customers, employees and production operations were relocated four times into increasingly larger spaces. Igus can change its production system at a moment's notice and with minimal disruption, and because the company operates seven days a week, 24 hours a day, these changes are occurring constantly.

To facilitate these changes, workers are equipped with power scooters so they can move around the plant quickly to reconfigure operations. The scooters also

allow them to move quickly to wherever in the factory their skills are most needed. Employees also carry mobile phones so they are always on call.

Igus's decision to create a flexible factory has paid off. In the last five years its sales have increased from \$10 million to \$100 million, and its global staff has tripled.

Just-in-time inventory and efficiency

inventory The stock of raw materials, inputs, and component parts that an organization has on hand at a particular time.

just-in-time inventory system

A system in which parts or supplies arrive at an organization when they are needed, not before.

Inventory is the stock of raw materials, inputs, and component parts that an organization has on hand at a particular time. Just-in-time (JIT) inventory systems play a major role in the process of identifying and finding the source of defects in inputs. When an organization has a **just-in-time inventory system**, parts or supplies arrive at the organization when they are needed, not before. Under a JIT inventory system, defective parts enter an organization's production system immediately; they are not warehoused for months before use. This means that defective inputs can be quickly spotted. Managers can then trace a problem to the supply source and fix it before more defective parts are produced.

JIT systems, such as Toyota's *kanban* system, were originally developed as part of the effort to improve product quality; they have major implications for efficiency. Toyota's system is based on the delivery of components to the production line just as they are needed. This leads to major cost savings from increasing inventory turnover and reducing inventory holding costs, such as warehousing and storage costs and the cost of capital tied up in inventory. Although companies that manufacture and assemble products can obviously use JIT to great advantage, so can service organizations. Wal-Mart, the biggest retailer in the United States, uses JIT systems to replenish the stock in its stores at least twice a week. Many Wal-Mart stores receive daily deliveries. Wal-Mart's main competitors, Kmart and Sears, typically replenish their stock every two weeks. Wal-Mart can maintain the same service levels as these competitors but at one-fourth the inventory-holding cost, a major source of cost saving. Faster inventory turnover has helped Wal-Mart achieve an efficiency-based competitive advantage in the retailing industry.¹⁷

One drawback of JIT systems is that they leave an organization without a buffer stock of inventory.¹⁸ Although buffer stocks of inventory can be expensive to store, they can help an organization when it is affected by shortages of inputs brought about by a disruption among suppliers (such as a labor dispute in a key supplier). Moreover, buffer stocks can help an organization respond quickly to increases in customer demand—that is, they can increase an organization's responsiveness to customers. Even a small company can benefit from a *kanban*, as the experience of United Electric suggests in the nearby "Management Insight."



Management Insight

United Electric's Kanban System

United Electric Controls, headquartered in Watertown, Massachusetts, is the market leader in the application of threshold detection and switching technology. Once the company simply warehoused its inputs and dispensed them as needed. Then it decided to reduce costs by storing these inputs at their point of use in the production system. However, this practice caused problems because inventories

of some inputs actually started to increase while other inputs were used up without anyone knowing which input caused a stoppage in production. Thus, managers decided to experiment with a supplier kanban system even though United Electric had fewer than 40 suppliers who were totally up-to-date with the company's input requirements.

Managers decided to store a three-week supply of parts in a central store-room, a supply large enough to avoid unexpected shortages.¹⁹ They began by asking their casting supplier to deliver inputs in kanbans and bins. Once a week, this supplier checks up on the bins to determine how much stock needs to be delivered the following week. Other suppliers were then asked to participate in this system, and now more than 35 of United Electric's major suppliers operate some form of the kanban system.

By all measures of performance, the results have been successful. Inventory-holding costs have fallen sharply. Products are delivered to all customers on time. And even new products' design-to-production cycles have dropped by 50 percent because suppliers are now involved much earlier in the design process, so they can supply new inputs as needed.

Self-managed work teams and efficiency

Another efficiency-boosting technique is the use of self-managed work teams (see Chapter 11).²⁰ The typical team consists of from 5 to 15 employees who produce an entire product instead of only parts of it.²¹ Team members learn all team tasks and move from job to job. The result is a flexible workforce because team members can fill in for absent co-workers. The members of each team also assume responsibility for work and vacation scheduling, ordering materials, and hiring new members—previously all responsibilities of first-line managers. Because people often respond well to being given greater autonomy and responsibility, the use of empowered self-managed teams can increase productivity and efficiency. Moreover, cost savings arise from eliminating supervisors and creating a flatter organizational hierarchy, which further increases efficiency.

The effect of introducing self-managed teams is often an increase in efficiency of 30 percent or more, sometimes much more. After the introduction of flexible manufacturing technology and self-managed teams, a GE plant in Salisbury, North Carolina, increased efficiency by 250 percent compared with other GE plants producing the same products.²²

Process reengineering and efficiency

process

reengineering The fundamental rethinking and radical redesign of business processes to achieve dramatic improvements in critical measures of performance such as cost, quality, service, and speed.

Think of the major activities of businesses as processes that take one or more kinds of inputs and create an output that is of value to the customer.²³ **Process reengineering** is the fundamental rethinking and radical redesign of business processes to achieve dramatic improvements in critical measures of performance such as cost, quality, service, and speed.²⁴ Customer relationship management, as introduced at Citibank (see the “Management Insight” on page 493), for example, can be thought of as a business process: Once a customer's order is received (the input), all the activities necessary to process the order are performed, and the ordered goods are delivered to the customer (the output). Process reengineering can boost efficiency because it eliminates the time devoted to activities that do not add value.



"IF YOU'LL JUST SIT TIGHT, I'LL DIVE BACK DOWN INTO THE PRODUCT SPECS, QUOTES AND SAMPLES TO FIND A CONTRACT FOR YOU TO SIGN."

As an example of process reengineering in practice, consider how Ford Motor Company used it. One day a manager from Ford was working at its Japanese partner Mazda and discovered quite by accident that Mazda had only five people in its accounts payable department. The Ford manager was shocked, for Ford's U.S. operation had 500 employees in accounts payable. He reported his discovery to Ford's U.S. managers, who decided to

form a task force to figure out why the difference existed.

Ford managers discovered that procurement began when the purchasing department sent a purchase order to a supplier and sent a copy of the purchase order to Ford's accounts payable department. When the supplier shipped the goods and they arrived at Ford, a clerk at the receiving dock completed a form describing the goods and sent the form to accounts payable. The supplier, meanwhile, sent accounts payable an invoice. Thus, accounts payable received three documents relating to these goods: a copy of the original purchase order, the receiving document, and the invoice. If the information in all three was in agreement (most of the time it was), a clerk in accounts payable issued payment. Occasionally, however, all three documents did not agree. Ford discovered that accounts payable clerks spent most of their time straightening out the 1 percent of instances in which the purchase order, receiving document, and invoice contained conflicting information.²⁵

Ford managers decided to reengineer the procurement process to simplify it. Now when a buyer in the purchasing department issues a purchase order to a supplier, that buyer also enters the order into an on-line database. As before, suppliers send goods to the receiving dock. When the goods arrive, the clerk at the receiving dock checks a computer terminal to see whether the received shipment matches the description on the purchase order. If it does, the clerk accepts the goods and pushes a button on the terminal keyboard that tells the database the goods have arrived. Receipt of the goods is recorded in the database, and a computer automatically issues and sends a check to the supplier. If the goods do not correspond to the description on the purchase order in the database, the clerk at the dock refuses the shipment and sends it back to the supplier.

Payment authorization, which used to be performed by accounts payable, is now accomplished at the receiving dock. The new process has come close to eliminating the need for an accounts payable department. In some parts of Ford, the size of the accounts payable department has been cut by 95 percent. By reducing the head count in accounts payable, the reengineering effort reduced the amount of time wasted on unproductive activities, thereby increasing the efficiency of the total organization.

In sum, managers at all levels have important roles to play in a company's effort to boost efficiency. Top management's role is to encourage efficiency improvements by, for example, emphasizing the need for continuous improvement

or reengineering. Top management also must ensure that managers from different functional departments work together to find ways to increase efficiency. However, while top managers might recognize the need for such actions, functional-level managers are in the best position to identify opportunities for making efficiency-enhancing improvements to an organization's production systems. They are the managers who are involved in an organization's production system on a day-to-day basis. Improving efficiency, like quality, is an ongoing, never-ending process.

Operations Management: Some Remaining Issues

Achieving superior responsiveness to customers through quality and efficiency often requires a profound shift in management operations and in the culture of an organization. Many reports have appeared in the popular press about widespread disillusionment with JIT, flexible manufacturing, and reengineering. It is possible that many of the disillusioned organizations are those that failed to understand that implementing these systems requires a marked shift in organizational culture.²⁶ None of

these systems is a panacea that can be taken once, like a pill, to cure industrial ills. Making these techniques work within an organization can pose a significant challenge that calls for hard work and years of persistence by the sponsoring managers.

Managers also need to understand the ethical implications of the adoption of many of the production techniques discussed here. JIT, flexible manufacturing, and reengineering can all increase quality, efficiency, and responsiveness to customers, but they may do so at great cost to employees. Employees may see the demands of their job increase, or, worse, they may see themselves reengineered out of a job. For example, Toyota is the most efficient car manufacturer in the world, but some of its gains have been achieved at a significant cost to its employees, as discussed in the following "Ethics in Action."



Ethics in Action

The Human Cost of Improving Productivity

Hisashi Tomiki is the leader of a four-man self-managed team in a Toyota production plant, 200 miles south of Tokyo, Japan. Tomiki and his team work at a grueling pace to build cowl (steel chambers onto which windshields and steering columns are attached). Consider this description of Tomiki at work:

In two minutes Tomiki fits 24 metal pieces into designated slots on three welding machines; runs two large metal sheets through each of the machines, which weld on the parts; and fuses the two sheets together with two spot welds. There is little room for error. Once or twice an hour a mistake is made or a machine sticks, causing the next machine in line to stop. A yellow light flashes. Tomiki runs over. The squad must fix the part and work faster to catch up. A red button halts the production line if the problems are severe, but there is an unspoken rule against pushing it. Only once this day does Tomiki call in a special maintenance worker.²⁷

The experience of workers like Tomiki has become increasingly common. Workers are heard to complain that constant attempts to increase quality and reduce costs really mean continuous speedup and added job stress from the increased pressure on employees to perform. Although some pressure is good, past a certain point it can seriously harm employees. Moreover, consider the following comment by Jerry Miller, a former employee of US West, whose team of billing clerks reengineered themselves out of a job: "When we first formed our teams, the company came in talking teams and empowerment and promised that we wouldn't lose any jobs. It turns out all this was a big cover. The company had us all set up for reengineering. We showed them how to streamline the work, and now 9,000 people are gone. It was cut-your-own-throat. It makes you feel used."²⁸

Is it ethical to continually increase the demands placed on employees, regardless of the human cost in terms of job stress? Obviously, the answer is no. Employee support is vital if an organization is to function effectively. What kinds of work pressures are legitimate, and what pressures are excessive? There is no clear answer to this question. Ultimately the issue comes down to the judgment of responsible managers seeking to act ethically.

Summary and Review

OPERATIONS MANAGEMENT AND COMPETITIVE ADVANTAGE

To achieve high performance, managers try to improve their responsiveness to customers, the quality of their products, and the efficiency of their organization. To achieve these goals, managers can use a number of operations management techniques to improve the way an organization's production system operates.

IMPROVING RESPONSIVENESS TO CUSTOMERS To achieve high performance in a competitive environment, it is imperative that the production system of an organization responds to customer demands. Managers try to design production systems that produce outputs that have the attributes customers desire. One of the central tasks of operations management is to develop new and improved production systems that enhance the ability of the organization to deliver economically more of the product attributes that customers desire for the same price. Techniques such as JIT, flexible manufacturing, and process reengineering are popular because they promise to do this. Managers should analyze carefully the links between responsiveness to customers and the production system of an organization. The ability of an organization to satisfy the demands of its customers for lower prices, acceptable quality, better features, and so on, depends critically on the nature of the organization's production system. As important as responsiveness to customers is, however, managers need to recognize that there are limits to how responsive an organization can be and still cover its costs.

IMPROVING QUALITY Managers seek to improve the quality of their organization's output because it enables them to better serve customers, to raise

prices, and to lower production costs. The attempt to improve quality requires an organizationwide commitment; managers emphasize a strong customer focus, find ways to measure quality, set quality improvement goals, solicit input from employees about how to improve product quality, and design products for ease of manufacture.

IMPROVING EFFICIENCY Improving efficiency requires one or more of the following: improve quality, adopt flexible manufacturing technologies, introduce just-in-time inventory systems, establish self-managed work teams, and use process reengineering. Top management is responsible for setting the context within which efficiency improvements can take place by, for example, emphasizing the need for continuous improvement. Functional-level managers bear prime responsibility for identifying and implementing efficiency-enhancing improvements in production systems.



Management in Action

Topics for Discussion and Action

1. Ask a manager how quality, efficiency, and responsiveness to customers are defined and measured in his or her organization.
2. Go into a local store, restaurant, or supermarket, and list the ways in which you think the organization is being responsive or unresponsive to the needs of its customers. How could this business's responsiveness to customers be improved?
3. What is efficiency, and what are some of the techniques that managers can use to increase it?
4. Why is it important for managers to pay close attention to their organization's production system if they wish to be responsive to their customers?
5. "Total customer service is the goal toward which most organizations should strive." To what degree is this statement correct?

Building Management Skills

Managing a Production System

Choose an organization with which you are familiar—one that you have worked in or patronized or one that has received extensive coverage in the popular press. The organization should be involved in only one industry or business. Answer these questions about the organization.

1. What is the output of the organization?
2. Describe the production system that the organization uses to produce this output.
3. What product attributes do customers of the organization desire?
4. Does its production system allow the organization to deliver the desired product attributes?
5. Try to identify improvements that might be made to the organization's production system to boost the organization's responsiveness to customers, quality, and efficiency.

Small Group Breakout Exercise

How to Compete in the Sandwich Business

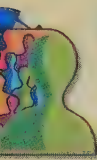
Form groups of three or four people, and appoint one member as the spokesperson who will communicate your findings to the whole class when called on by the instructor. Then discuss the following scenario.

You and your partners are thinking about opening a new kind of sandwich shop that will compete head-to-head with Subway and Thundercloud Subs. Because these chains have good brand-name recognition, it is vital that you find some source of competitive advan-

tage for your new sandwich shop, and you are meeting to brainstorm ways of obtaining one.

1. Identify the product attributes that a typical sandwich shop customer most wants.
2. In what ways do you think you will be able to improve on the

operations and processes of existing sandwich shops and achieve a competitive advantage through better (a) product quality, (b) efficiency, or (c) responsiveness to customers?



Be the Manager

You are an operations management consultant who has been called in by the management team of a start-up company that will produce flat screen displays for personal computer manufacturers like Dell and Compaq. The flat screen display market is highly competitive; there is considerable pressure to reduce costs because prices fall rapidly due to competition. Also, personal computer makers are demanding ever higher quality and

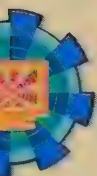
better features to please customers, and they demand delivery of your product to meet their production schedules. Managers want your advice on how to best meet these requirements. They are in the process of recruiting new workers and building a production facility.

Questions

1. What kinds of techniques discussed in the chapter can

help these managers to increase efficiency?

2. In what ways can these managers go about developing a program to increase quality?
3. What critical lessons can these managers learn from operations management?



Additional Activities on the Build Your Management Skills DVD

- **Test Your Knowledge:**
 - (a) Project Planning and
 - (b) Facilities Layout
- **Manager's Hot Seat:**

Virtual Workplace: Out of Office Reply



Managing Ethically

Review "Ethics in Action: The Human Cost of Improving Productivity." After the implementing of many operations management techniques, layoffs occur in many companies, and, frequently, employees must perform more tasks more quickly, which can generate employee stress and other work-related problems.

Questions

1. Either by yourself or in a group, discuss how to think through the ethical implications of using a new operations management technique to improve organizational performance.
2. What criteria would you use to decide what kind of technique

it is ethical to adopt and how far to push employees to raise the level of their performance?

3. How big a layoff, if any, would be acceptable? If layoffs are acceptable, what could be done to reduce their harm to employees?



Case in the News

A "China Price" For Toyota

Five years ago, Toyota Motor Corp. (TM) stunned the auto world by embarking on a plan to slash costs 30 percent across the board for the car parts it buys—from air-conditioning ducts and door-assist grips to windshield

wipers. The bold plan to squeeze its own network of traditional suppliers, known as a *keiretsu*, was designed to make sure the Toyota group would retain its competitive edge against a spate of global auto alliances such as DaimlerChrysler

(DCX), which promised gigantic synergies from their big size.

DaimlerChrysler is still struggling to make its merger pay off. But Toyota's cost-cutting program—dubbed CCC21, or Construction of Cost Competitiveness for the 21st

century—has been a remarkable success. With just one year to go, the plan is on track to save the auto maker some \$10 billion over its five-year time frame. Not only is CCC21 sourcing components more cheaply but Toyota has also improved the parts' quality. The program has even bested archrival Nissan Motor Co. (NSANY), whose chief executive, Carlos Ghosn, kicked off the savings scramble in 1999 by pledging 20 percent cuts in procurement costs.

But where does Toyota go from here? Even after putting its supply network through the wringer, Japan's number one carmaker can ill afford to rest easy. Toyota may be under more pressure now to cut costs than when it began CCC21. So the drive is on to replace expensive materials, benchmark Toyota's auto parts against Chinese-level pricing, and squeeze its Japanese suppliers further by relying more on non-*keiretsu* parts makers. "We need to adjust our cost-cutting drive to meet a whole new set of challenges," says Katsuaki Watanabe, 62, the executive vice-president who helped devise and supervise CCC21. In a sign that streamlining is still a top priority, the company announced on February 9 that Watanabe will take over as president of Toyota from Fujio Cho in June.

Steel Shortage

Watanabe is a demon at spotting costs that no one even knew existed and eliminating redundancies that few had noticed. Under his prodding, one Toyota CCC21 team disassembled the horns made by a Japanese supplier and found ways to eliminate six of 28 components, resulting in a 40 percent cost reduction. No part has been too mundane to escape the Watanabe squad's notice. His favorite exam-

ple: interior assist grips above each door. There once were 35 different grips. Now, Toyota's entire 90-model lineup uses just three basic styles. Toyota gearheads call this process *kawaita zokin wo shiboru*, or "wringing drops from a dry towel." It is an unending, excruciating process, but essential to Toyota's bottom line.

But even Watanabe needs a new game plan to counter what is coming. Among the most pernicious threats: the surge in prices of crucial items such as sheet steel due to higher costs for raw materials like iron ore and coal. Blame China's voracious demand for steel and a shortage of Asian blast furnace capacity—factors that are unlikely to go away anytime soon. What is more, the strong yen means Toyota's reported profits from outside Japan come in lower, increasing the pressure to cut expenses.

These burdens come just as the automotive giant's latest cost-cutting push has started to run out of steam. On February 3 the company acknowledged its cost cuts will likely total just \$1.7 billion for the fiscal year ending in March, 15 percent short of its annual target, in large part because of the surge in sheet steel prices. Nikko Citigroup Ltd. notes that the pace of cost cuts has slowed to \$388 million in the most recent quarter, down from \$582 million a year earlier.

To cope, Watanabe is pushing Toyota to winnow down the number of steel parts it uses in an average vehicle from 610 to about 500, although it won't say by when or how much savings that will net. Toyota will probably turn to more steel substitutes such as aluminum and heavy-duty advanced plastics and resins. Moving away from steel goes hand-in-hand with the company's longer-term goal of cutting

the weight of its vehicles to increase fuel efficiency and rust-proof durability.

That said, there's a limit to how many steel parts Toyota can replace. There is also no guarantee that prices of aluminum and petrochemicals will not skyrocket to the point where those materials are no longer cost-effective substitutes.

Something more is needed—and that is the China benchmark. Under CCC21, Watanabe's lieutenants identified about 180 key parts, then figured out who the world's most competitive suppliers of those parts were—companies like Robert Bosch of Germany, Delphi Corp. (DPH), and the Toyota Group's own Denso Corp. The Toyota cost-cutters used this information as the "benchmark" against which Toyota's *keiretsu* suppliers had to compete. The *keiretsu* outfits must learn how to meet the benchmark—or risk losing the business. Toyota worked with affiliate Denso, for example, to consolidate production of air-conditioning vents to just four key styles, down from 27 previously. That resulted in a 28 percent cost reduction. Watanabe still was not happy: He had wanted just three.

Now the exercise goes to a whole new level. The boom in auto production in China is nurturing a car-parts industry with both multinational suppliers and local companies providing new data on how low prices can go. For now, that is mostly limited to commodity-type components such as assist grips, not high-end modules and core parts like brakes. Toyota officials say the rise of China has raised the bar for its *keiretsu* suppliers. They increasingly must push their prices toward the Chinese level to keep Toyota's business. "China has become an important new benchmark for us," says Watanabe.

This doesn't mean Toyota will soon start importing all its parts from China for use in its Japanese and U.S. factories. Analysts say it may be a decade before the parts makers in China can go toe-to-toe with components made in Japan, South Korea, and the United States. The ultralow defect rates for parts made in Japan, for example, can be as important to cutting prices as cheap fixed costs. Even so, benchmarking against the Chinese price forces suppliers to come as close as possible to matching it without sacrificing quality. That involves rethinking everything, from the number of designers assigned to making any one part, to the supply chain involved in sourcing components, to the utilization rates of equipment at a parts factory.

The China benchmark will increase the pressure on Toyota's traditional suppliers. But so will the company's efforts to court more non-Japanese suppliers to find the best price. And parts makers like Bosch and Delphi, which turn out everything from air bags to transmissions, are now more willing to meet demanding specifications. Bosch, for example, supplies the complete brake system for the Toyota Avenis sedan and the diesel-injection system for the Toyota Yaris subcompact, both made in Europe. Toyota won't

say how much of its parts purchasing comes from its *keiretsu* versus outsiders, but non-Japanese suppliers are eager to win a bigger share. No wonder: The auto maker expects its global sales to hit 8.5 million vehicles by next year, about 1 million more than in 2004. That will put it on par with General Motors Corp. (GM), the world's largest carmaker. "Toyota is an important customer for Bosch," says Bernd Bohr, chairman of the company's automotive group. "We maintain a close cooperative relationship with Toyota and in development projects."

Non-*keiretsu* suppliers see their best chance in markets where Toyota is expanding fastest, especially China, where the Japanese auto maker is eager to catch up with established rivals like GM and Volkswagen. "This is a great opportunity for outside suppliers to increase their business with us," says Watanabe. Those suppliers would love ultimately to win orders on a global basis—including in Japan, where local suppliers account for all but a fraction of the auto giant's parts purchases.

Part of the Family

To show the depth of its commitment, Delphi now sends technicians to Toyota headquarters in Toyota City to collaborate on the

blueprints for new parts, and invites Toyota execs to tour its plants and offer suggestions for improving productivity and increasing quality. Although Delphi won't disclose how much business it does with Toyota, less than 10 percent of its roughly \$1 billion in Asian revenue comes from the Japanese. The company, however, says it has high hopes for supplying more to Toyota from its 13 plants in China. "We are becoming part of Toyota's extended *keiretsu* family," says Choon T. Chon, president of Delphi's Asia Pacific unit. And part of Watanabe's ruthless drive to cut costs to the bone.

Questions

1. In what ways did Toyota's CCC21 plan improve the efficiency of its operations and materials management process?
2. In what ways is Toyota continuing to find ways to increase efficiency?
3. In what ways is low-cost Chinese competition helping Toyota reduce its OMM costs?

Source: C. Dawson and K. Nickel Anhalt, "A China Price For Toyota." Reprinted from the February 21, 2005, issue of *BusinessWeek* by special permission. Copyright © 2005 by the McGraw-Hill Companies, Inc.

Time was, Japan had a well-deserved reputation as a black hole for foreign retailers. Its close-knit webs of suppliers, customers raised on high-cost department stores and mom-and-pop shops, and a Byzantine distribution system made Japan nearly impenetrable to outsiders. Three years ago, though,

Wal-Mart Stores Inc. (WMT) bought a stake in struggling Seiyu Ltd. as relaxed restrictions on retailers and changing consumer attitudes appeared to create an opening for its big box stores.

Today it looks as if Japan may not have changed so much after all. Seiyu—in which Wal-Mart owns a

controlling 37 percent share—on February 15 reported a loss for 2004 of \$117 million, more than triple its earlier projections. Revenues, meanwhile, slipped by 3.7 percent, to \$9.8 billion. Worse, the decline seems to be accelerating: Sales tumbled by 5.7 percent in the second half, compared with a

3.5 percent drop in the first. Blaming the shortfall on unseasonable weather, stiff competition from rivals, and difficulties with new computer systems, Seiyu says it expects sales to fall a further 2 percent this year. "Clearly we're disappointed with the results," says Jeff McAllister, Wal-Mart Japan's chief operating officer. "We recognize that with the changes we have been through, we created some confusion for our associates and our customers." Profits, meanwhile, are not likely before 2006, Seiyu says. Investors do not like the sound of that, and Seiyu's shares are off by 31 percent in the past 12 months.

Just as worrisome is that Seiyu remains far from offering the storewide, permanent discounts that have made Wal-Mart so dominant in the United States. Seiyu says full implementation of Wal-Mart's Every Day Low Prices—which everyone at the company refers to as "EDLP"—is at least two years away because the company has not yet been able to cut costs enough to allow it to offer the deep discounts necessary to keep customers coming back. And Seiyu continues to use *chirashi*, newspaper inserts that are a staple of Japanese retail outlets. They offer a handful of weekly specials but otherwise keep prices relatively high. That is anathema to Wal-Mart and its EDLP mantra. The company says, though, that it will keep on using the flyers until customers no longer require wooing.

Suspicious

Some are wondering whether the Wal-Mart model will ever work in Japan. "The current situation suggests that [EDLP] is a very difficult target," says Masafumi Shoda, a retail analyst at Nomura Securities Co. (NMR) in Tokyo. One big prob-

lem is that Japanese customers do not seem as motivated by rock-bottom prices as Americans. U.S. shoppers generally believe Wal-Mart sells the same products as other stores but for 15 percent to 20 percent less. In Japan, shoppers associate low prices with low quality and are suspicious when a retailer offers jeans for \$10. "In the Japanese consumer mind, they are seen as selling cheap stuff at cheap prices—and that can be a problem," says David Marra, a principal at management consultancy A.T. Kearney Inc. in Tokyo.

It is also tough for Seiyu to take more costs out of its supply chain—a key to Wal-Mart's success in the United States. Seiyu stores combine the functions of a supermarket with those of a mid-level department store. One big issue for the supermarket side is that Japanese consumers buy more fresh produce than shoppers elsewhere. That makes lowering costs difficult since most farms and fisheries in Japan are small, family-run operations that frequently offer better deals on smaller orders rather than on larger ones. And what sells well in Hokkaido is often eschewed in Kyushu, so retailers have to do lots of local customization, which creates logistical headaches that can cut into profits.

To be fair, Wal-Mart is not alone in its troubles. Even though convenience stores and specialty retailers are thriving, big-box outlets continue to flounder. Aeon Co., Japan's largest retailer, has struggled to make the leap to storewide low prices as well. To cut costs, Aeon has sunk more than \$300 million into new computer systems in the past two years and has attempted to use its size to bypass middlemen. Yet Nomura reckons that Aeon's general retail arm, which accounts for 43 percent of

group sales, will contribute only \$228 million toward group operating profits in fiscal 2004, just 15 percent of the total. Its other businesses—from credit cards to convenience stores—are far more profitable.

Up from \$10 Jeans

Aeon President Motoya Okada admits that changing to a Wal-Mart model is taking longer than expected. "We are two or three years behind in our plans," he says. "We have not yet caught up with our vision." Meanwhile, Carrefour, the world's second-largest retailer, is widely rumored to be looking for a buyer for its eight hypermarkets in Japan after failing to make an impact with Japanese shoppers. Carrefour declined to comment. Daiei, another icon of Japanese retailing, remains deeply troubled and is in the hands of Japan's state bad-debt agency.

Seiyu promises that better news is just around the corner. The company says it has cut costs by 6.1 percent by trimming payrolls, reducing distribution expenses, and scaling back advertising. And it has installed Wal-Mart's computer systems in more than half its 400 stores. The technology lets Seiyu see exactly what customers are buying and what remains on store shelves, helping managers track inventory better. "This is a real competitive advantage," McAllister says. "We'll take the systems and continue to roll them out to get a better insight into consumer spending habits."

To head off any concerns that its bargain prices mean low quality, Seiyu is adding more expensive wares. For example, it is supplementing its current range of \$10 jeans with a \$35 option for less price-conscious customers. Similarly, Seiyu stores is offering

100 percent cotton dress shirts for as much as \$28—in addition to the cotton/polyester blends costing as little as \$8 it has specialized in so far. Wal-Mart also plans to spruce up about 20 of Seiyu's stores, many of which look frumpy. Seiyu says a 4,800-square-meter outlet in the Tokyo suburb of Saitama saw customers increase by 35 percent after the layout was improved and product mix revamped in a renovation last year.

For Seiyu and its 36,000 workers, Wal-Mart may be the last, best hope. When Wal-Mart bought in, profits were plunging as the company reached too far beyond its core su-

permarket business. "Everyday Low Prices cannot be achieved overnight, but we have to meet the challenge," Seiyu President Masao Kiuchi told reporters on February 15. "Otherwise, there will be no rebirth of Seiyu." For Wal-Mart, success in Japan is almost as important, since a solid foothold in the world's number two retail market could someday be a key to future growth. But even McAllister will not say exactly when Seiyu will get to U.S.-style EDLP in Japan. Until it does, it will remain unclear whether Japanese retailing has really changed enough to make room for Wal-Mart.

Questions

1. Why do Japanese retailers believe it would be too difficult to copy Wal-Mart's efficient operations processes?
2. Wal-Mart wants to enter the Japanese market. Why do its managers believe they will be able to transplant Wal-Mart's efficient operating system to Japan?

Source: I. Rowley, "Japan Isn't Buying the Wal-Mart Idea." Reprinted from the February 28, 2005, issue of *BusinessWeek* by special permission. Copyright © 2005 by the McGraw-Hill Companies, Inc.

Career Development

APPENDIX B

career The sum total of work-related experiences throughout a person's life.

Managers face several challenges both in the course of their own careers and in facilitating effective career management for their subordinates. A **career** is the sum total of work-related experiences throughout a person's life.¹ Careers encompass all of the different jobs people hold and the different organizations they work for. Careers are important to most people for at least two reasons. First, a career is a means to support oneself and one's loved ones, providing basic necessities and opportunities to pursue outside interests. Second, a career can be a source of personal fulfillment and meaning. Many managers find that making a difference in an organization and helping improve organizational efficiency and effectiveness are personally as well as financially rewarding.

Career development is a concern for managers both in terms of how their own careers unfold over time and how careers are managed in their organizations. In the development of their own careers, managers seek out challenging and interesting jobs that will develop their skills, lead to future opportunities, and allow them the opportunity to do the kind of work that will be personally meaningful. Similarly, in motivating and leading subordinates, managers need to be attuned to subordinates' career development. When careers (of both managers and rank and file employees) are effectively managed in an organization, the organization makes the best use of its human resources and employees tend to be motivated by, and satisfied with, their jobs.

Both employees and managers play an important role in effectively managing careers. For example, employees need to understand themselves, the kind of work they find motivating and fulfilling, and their own future aspirations for their careers. Employees then need to proactively seek the education, training, and kinds of work experiences that will help them to have the career they want. Managers can motivate employees to make meaningful contributions to organizations by providing them with work assignments, experiences, training, and opportunities that contribute to employees' career development.²



eBay CEO Margaret (Meg) Whitman served in different posts for an array of companies, such as Stride Rite, FTD, Procter & Gamble, Disney, and Hasbro, before finding her niche at the successful online auction company.

Types of Careers

While every person's career is somewhat unique, the different types of careers that people have fall into four general categories: steady-state careers, linear careers, spiral careers, and transitory careers.³

steady-state career

A career consisting of the same kind of job during a large part of an individual's work life.

STEADY-STATE CAREERS A person with a **steady-state career** makes a one-time commitment to a certain kind of job that he or she maintains throughout his or her working life.⁴ People with steady-state careers can become very skilled and expert at their work. A playwright who starts writing plays upon graduation from college and continues to write plays until retiring at age 70 has a steady-state career. So too does a dentist who maintains a steady dental practice upon graduation from dental school until retirement.

Some managers choose to have a steady-state career, holding the same kind of job during a large part of their work life, often becoming highly skilled and expert in what they do. A talented and creative graphic artist at a magazine publishing company, for example, may turn down promotions and other "opportunities" so that he can continue to work on designing attractive magazine spreads and covers, what he really likes to do. Similarly, some managers at Dillard's have steady-state careers as area sales managers because they enjoy the direct supervision of salespeople and the opportunity to "stay close to" customers.

linear career

A career consisting of a sequence of jobs in which each new job entails additional responsibility, a greater impact on an organization, new skills, and upward movement in an organization's hierarchy.

LINEAR CAREERS A person who has a **linear career** moves through a sequence of jobs in which each new job entails additional responsibility, a greater impact on an organization, new skills, and upward movement in an organization's hierarchy.⁵ The careers of many managers are linear, whether they stay with the same company or frequently switch organizations. A linear career traces a line of upward progress in the positions held.

Top managers in large corporations like Margaret Whitman, CEO of eBay, and Robert Nardelli, CEO of Home Depot,⁶ moved through a series of lower level positions in a variety of organizations before they became CEOs. Similarly, the assistant manager at the Red Lobster in College Station, Texas, started out in an entry-level position as a cashier. A linear career at Dillard's department stores may include the following sequencing of positions: executive trainee, area sales manager, assistant buyer, buyer, assistant store manager of merchandising, store manager, and divisional merchandise manager.⁷ Managers' subordinates also may have linear careers, although some subordinates may have other types of careers.

spiral career

A career consisting of a series of jobs that build on each other but tend to be fundamentally different.

SPIRAL CAREERS A person who has a **spiral career** tends to hold jobs that, while building off of each other, tend to be fundamentally different.⁸ An associate professor of chemical engineering who leaves university teaching and research to head up the R&D department of a chemical company for 10 years and then leaves that position to found her own consulting firm has a spiral career. Similarly, a marketing manager in a large corporation who transfers to a job in public relations and then, after several years in that position, takes a job in an advertising firm has a spiral career. Those three jobs tend to be quite different from each other and do not necessarily entail increases in levels of responsibility.

transitory career

A career in which a person changes jobs frequently and in which each job is different from the one that precedes it.

TRANSITORY CAREERS Some people change jobs frequently and each job is different from the one that precedes it; this kind of career is a **transitory career**.⁹ A middle school teacher who leaves teaching after two years to work as an

administrative assistant in a consumer products company for a year and then moves on to do carpentry work has a transitory career.

Career Stages

While every person's career is somewhat unique, there are certain career stages that at least some people appear to progress through. Even if a person does not progress through all the stages, typically some of the stages are experienced. Each stage is associated with certain kinds of activities, hurdles, and potential opportunities. Regardless of the extent to which a person experiences each stage, and regardless of the exact number of the stages about which there is some disagreement among researchers, here we discuss five stages (see Exhibit A) that are useful to understand and manage careers.¹⁰

These career stages apply to managers and nonmanagers alike. Thus, understanding the stages is important for managers both in terms of their own career development and in terms of the career development of their subordinates. Importantly, and increasingly, these career stages are experienced by most people in a variety of organizations. That is, while in the past, at least some people might have spent most of their careers in a single organization (or in just a few organizations), this is becoming increasingly rare. Rapid changes in technology, increased global competition, environmental uncertainty, outsourcing, and the layoffs many organizations resort to at one point or another to reduce costs are just some of the factors responsible for people's careers unfolding in a series of positions in a number of different organizations. Thus, a **boundaryless career**, or a career that is not attached or bound to a single organization, is becoming increasingly common and most people have a variety of work experiences in multiple organizations throughout their careers.¹¹

boundaryless career A career that is not attached to or bound to a single organization and consists of a variety of work experiences in multiple organizations.

PREPARATION FOR WORK During this stage, people decide what kind of career they desire and learn what qualifications and experiences they will need in order to pursue their chosen career.¹² Deciding on a career is no easy task and requires a certain degree of self-awareness and reflection. Sometimes people turn to professional career counselors to help them discover the kinds of careers in which they are most likely to be happy. A person's personality, values, attitudes, and moods impact the initial choice of a career.¹³

After choosing a career area, a person must gain the knowledge, skills, and education necessary to get a good starting position. A person may need an undergraduate or graduate degree or may be able to acquire on-the-job training through an apprenticeship program (common in Germany and some other countries).

ORGANIZATIONAL ENTRY At this stage, people are trying to find a good first job. The search entails identifying potential opportunities in a variety of ways (such as reading advertisements, attending career/job fairs, and mining personal



Exhibit A
Career Stages

contacts), finding out as much as possible about alternative positions, and making oneself an attractive candidate for prospective employers. Organizational entry is a more challenging stage for some kinds of careers than for others. An accounting major who knows she wants to work for an accounting firm already has a good idea of her opportunities and of how to make herself attractive to such firms. An English major who wants a career as an editor for a book publisher may find entry-level positions that seem a “good” start to such a career few and far between and may decide her best bet is to take a position as a sales representative for a well-respected publisher. More often than not, managers do not start out in management positions but rather begin their careers in an entry-level position in a department such as finance, marketing, or engineering.

EARLY CAREER The early-career stage begins after a person obtains a first job in his or her chosen career. At this stage there are two important steps: establishment and achievement. *Establishment* means learning the ropes of one’s new job and organization—learning, for example, specific job responsibilities and duties, expected and desired behaviors, and important values of other organizational members such as the boss.¹⁴ A person who has acquired the basic know-how to perform a job and function in the wider organization is ready to take the second step. *Achievement* means making one’s mark, accomplishing something noteworthy, or making an important contribution to the job or organization.¹⁵

The achievement step can be crucial for future career progression. It is a means of demonstrating one’s potential and standing out from others who are aspiring to become managers and are competing for desired positions. Downsizing and restructuring have reduced the number of management positions at many large companies, making it very important for individuals to manage the early-career stage effectively and thus increase their chances of advancement. By identifying where and how you can make a truly significant contribution to an organization, you can enhance your career prospects both inside and outside the organization.

Increasing numbers of Americans at this stage are working abroad to make their significant achievements—in regions as diverse as eastern Europe, Southeast Asia, and Latin America and in cities such as Budapest and Hong Kong. And their bold decisions seem to be paying off. When Daniel Arbess was an associate at the prestigious New York law firm White & Case, he worked in the late 1980s and early 1990s in Czechoslovakia, trying to gain the legal account of Skoda Auto Co. for his firm, and eventually he succeeded. Volkswagen subsequently invested \$6.4 billion in Skoda, which greatly increased the volume of Skoda’s legal work, which White & Case was asked to perform. Arbess’s work overseas not only enabled him to make a significant achievement at the early-career stage but also earned him the position of partner at White & Case.

Some people find that seeking out and gaining the assistance of a mentor can be a valuable asset for the early-career and subsequent stages. A **mentor** is an experienced member of an organization who provides advice and guidance to a less-experienced worker (the protégé, or mentee). The help that a mentor provides can range from advice about handling a tricky job assignment, dealing with a disagreement with a supervisor, and what kind of subsequent positions to strive for, to information about appropriate behavior and what to wear in various situations. Mentors often seek out protégés, but individuals also can be proactive and try to enlist the help of a potential mentor. Generally, especially good potential mentors are successful managers who have had a variety of experiences, genuinely desire to

mentor An experienced member of an organization who provides advice and guidance to a less-experienced worker.

help junior colleagues, and are interpersonally compatible with the would-be protégé. Research has found that receiving help from a mentor is associated with an increase in pay, pay satisfaction, promotion, and feeling good about one's accomplishments.¹⁶

MIDCAREER The midcareer stage generally occurs when people have been in the workforce between 20 and 35 years. Different managers experience this stage in quite different ways. For Steve Jobs of Apple Computer and Bill Gates of Microsoft, the midcareer stage is a high point—a time of major accomplishment and success. For other managers, the midcareer stage is a letdown because their careers plateau.

career plateau A position from which the chances of being promoted or obtaining a more responsible job are slight.

Managers reach a **career plateau** when their chances of being promoted into a higher position in their current organizations or of obtaining a more responsible position in another organization dwindle.¹⁷ Some managers inevitably will experience a career plateau because fewer and fewer managerial positions are available as one moves up an organization's hierarchy. In some organizations upper-level positions are especially scarce because of downsizing and restructuring.

Plateaued managers who are able to come to terms with their situation can continue to enjoy their work and make important contributions to their organization. Some plateaued managers, for example, welcome lateral moves, which give them the chance to learn new things and contribute in different ways to the organization. Some find being a mentor especially appealing and a chance to share their wisdom and make a difference for someone starting out in their field.

LATE CAREER This stage lasts as long as a person continues to work and has an active career. Many managers remain productive at this stage and show no signs of slowing down. William Dillard, the founder of Dillard's department stores, and Gwen Mellon, a major fund-raiser and supporter of the Albert Schweitzer Hospital in Haiti, continued to be productive when they were well into their 80s.

Effective Career Management

effective career management

Ensuring that at all levels in the organization there are well-qualified workers who can assume more responsible positions as needed.

Managers face the challenge of ensuring not only that they have the kind of career they personally desire but also that effective career management exists for all employees in their organization. **Effective career management** means that at all levels in the organization there are well-qualified workers who can assume more responsible positions as needed and that as many members of the organization as possible are highly motivated and satisfied with their jobs and careers. As you might imagine, effectively managing careers in a whole organization is no easy task. At this point, however, it is useful to discuss two important foundations of effective career management in any organization: a commitment to ethical career practices and accommodations for workers' multidimensional lives.

COMMITMENT TO ETHICAL CAREER PRACTICES Ethical career practices are among the most important ingredients in effective career management and, at a basic level, rest on honesty, trust, and open communication among organizational members. Ethical career practices include basing promotions on performance, not on irrelevant considerations such as personal friendships and ties, and ensuring that diverse members of an organization receive the career opportunities they deserve. Supervisors must never abuse their power to make career decisions affecting others and must never behave unethically to advance their own careers.

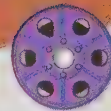
Managers at all levels must abide by and be committed to ethical career practices and actively demonstrate this commitment; they must communicate that violation of these practices will not be tolerated; and they must make sure that organizational members who feel that they were not ethically treated can communicate their concerns without fear of retaliation.

ACCOMMODATIONS FOR WORKERS' MULTIDIMENSIONAL LIVES

Effectively managing careers also means being sensitive to and providing accommodations for the multiple demands that many organizational members face in their lives. The dual-career couple is now the norm rather than the exception, the number of single parents is at an all-time high, and more and more midcareer workers need to care for their elderly and infirm parents. By limiting unnecessary moves and travel, adopting flexible work arrangements and schedules, providing on-site day care, and allowing workers to take time off to care for children or elderly parents, managers make it possible for workers to have satisfying and productive careers while fulfilling their other commitments.

Ernst & Young, for example, gives workers the choice of part-time work or flex-time work (full-time work scheduled to be convenient for a worker's personal life). Workers who have taken advantage of these options at Ernst & Young include Keeca, who after adopting three children from age 4 to 9 switched to a flexible schedule (flex-time work); Nancy, with a new daughter, who works three days in the office and is available on an as-needed basis at home the other two days; and Al, whose flex-time work allows him to help out at his son's cooperative preschool.¹⁸ By making accommodations for workers' multidimensional lives, managers not only help organizational members to have satisfying and productive careers but also help the organization to achieve its goals.

Careers are as important for managers' subordinates as they are for managers themselves. Understanding the many issues involved in effectively managing careers helps ensure that both managers and their subordinates will have the kinds of careers they want while helping an organization achieve its goals.



Chapter 1 Video Case: Wild Oats

Wild Oats Market is a supermarket with a difference. Since its start in Boulder, Colorado in 1987, Wild Oats has been committed to offering fresh, affordable natural and organic foods and providing knowledgeable customer service that goes beyond selling into consumer education. As it has grown, Wild Oats has reaped a reputation for being environmentally conscious, socially responsible and people-oriented.

Wild Oats sprung up as strong consumer interest in healthy eating developed. Demand for natural foods grew during the 1990s and continues to rise amid concerns about pesticides, fertilizers, artificial ingredients, and genetically altered food. With sales topping \$21 billion in 2004, natural and organic foods are moving from a niche category into the mainstream.¹ With more than 100 stores in 25 U.S. states and Canada, Wild Oats is the second largest retailer of natural and organic foods.

Since Perry Odak became CEO in 2001, Wild Oats has undergone massive restructuring to evolve from a company put together by various acquisitions to one with a consistent and profitable store base. Wild Oats planned to open 20 stores in 2005 and 40 the next year.² To increase profit margins, it has developed a private-label strategy. The company has rolled out hundreds of products under its own brand in its own stores and has tested the brand in a “store within a store” concept at a few outlets operated by other retailers. Wild Oats also has experimented with offering its private-label products online.³

Wild Oats stores are designed to offer a customer-friendly shopping experience. A new store in Superior, Colorado, stands as the model outlet. It uses color and attention-getting graphics for a fresh, dynamic feel. The center of the store is open and inviting with low shelves that allow customers an unobstructed view from any area. Educational opportunities abound, including a demonstration kitchen with seating and an information center in the health and beauty aids department.⁴

Focusing on the customer ranks at the top of Wild Oats’ values. The service expectations are higher than at traditional supermarkets, explains Peter Williams. Customers at Wild Oats’ stores typically have questions, and employees must be able to answer them. The company is careful to hire people who are committed to providing service and to giving them the expertise they need. Employee training begins with a full-day orientation centering on the company’s mission and values and how to live up to them. Then employees take a month-long course (and written test) in natural foods and receive hands-on training. While some employees were customers first before joining the staff, others were unfamiliar with natural and organic foods but were eager to learn. Once on board, Wild Oats employees share the belief that they make a difference in the health and lives of customers.

Communicating information, ideas, and concerns helps build trust and teamwork at Wild Oats. Experienced employees help new ones learn about the products. The company has an open door policy

that extends all the way to the top. Its Ethics Line is an online forum available for employees to give input—anonously—on what they see as unethical behavior.

A recent Work Life Survey, available to all employees, provided managers with lots of useful feedback and insight into why staffers like or dislike working at Wild Oats. The number one reason employees cited for working there: the company’s mission and values, which they share. Among the values is giving back to the community. Each Wild Oats store chooses small, local charities to support, and the company reimburses full-time employees for up to 52 hours of volunteer work a year. Carrying out its mission of service, Wild Oats was named one of “100 Best Corporate Citizens” by *Business Ethics* magazine and was the highest-ranking food retailer on the list.

Questions for Discussion

1. Which of the four building blocks of competitive advantage—efficiency; quality; speed, flexibility, and innovation; and responsiveness to customers—are discussed in the case? What is Wild Oats doing to improve its organization in these areas?
2. In what ways do Wild Oats managers perform the managerial functions—planning, organizing, leading, and controlling?
3. Why are managers essential to the success of an organization like Wild Oats?

Appendix A Video Case: The Evolution of Management

Since its emergence more than a century ago, after the industrial revolution, the field of management thought has expanded and changed to reflect societal, political, and economic influences. Characterized by four approaches—classical, behavioral, systems, and contingency—management thought has continuously impacted the workplace.

The industrial revolution saw sweeping changes—factories, large labor forces, dependence on machinery, and mass production of goods. By the late 1800s, U.S. business efficiency was not keeping pace with advances in assembly-line technology. Owners and managers grappled with new issues: workers' fear of losing jobs to machines and fear of the machines themselves; lack of experience in operating large factories; and the need for new authority structures. These issues were addressed by the two-pronged classical approach, consisting of scientific management and administrative management.

Scientific management was spurred by the work of Frederick Taylor, a major influence on management thought in the early 1900s. In the Philadelphia steel mills, Taylor witnessed “soldiering,” whereby employees deliberately slowed production so that management would not know the speed at which the work could be done. Taylor concluded that management’s failure to pay attention to workers caused the productivity problems, and he defined

management’s role in four points, based on standardization. The manager, said Taylor, is to (1) determine the single best way to perform a given task, (2) scientifically select and teach each worker, (3) cooperate with workers and give incentives to make sure tasks are performed the one best way, and (4) divide work and responsibility between management and workers.

In contrast to scientific management, administrative management’s focus is on organizing the work of a whole organization rather than concentrating on individual workers. This branch of the classical approach holds that the management function can be applied to any organization regardless of size or type.

The classical approach assumes that work is a rational activity that people engage in to make money; thus, their behavior on the job is predictable and easily comprehended—an assumption that is not always the case. In the 1920s and 1930s, the behavioral approach took management in a different direction. A famous behavioral study headed by Elton Mayo took place over nine years at Western Electric’s Hawthorne Plant in Chicago. Researchers who experimented with working conditions, such as changes in light levels, hours worked, rest periods, and incentives, found that such conditions had no direct effect on productivity but that good social relationships at work did.

In the 1950s, the systems approach brought a view of the organization as a set of interrelated parts—inputs, the transformation process, outputs, and feedback—that should be managed as one entity to reach a common objective. Integrating earlier theories, W. Edwards Deming championed “total quality,” which calls for continuous improvements and statistical process control to increase quality.

The systems approach led to the contingency approach, which recognized the need to consider an organization’s external environment and to adapt. This approach calls for managers to identify important factors in specific situations, look at how factors are intertwined, and determine causes and effects of management decisions.

Questions

1. Among his contributions to management thought, Frederick Taylor outlined the roles of a manager. Are these roles still relevant today? Explain.
2. What change in the direction of management theory and practice did the Hawthorne studies prompt?
3. Compare scientific management, as developed by Frederick Taylor, and management science theory, as espoused by W. Edwards Deming.

Chapter 2 Video Case: Toying with Success: The McFarlane Companies

Todd McFarlane, president and CEO of the McFarlane Companies, is an entrepreneur who understands the importance of product

development. Comics, sports, toys, and rock-and-roll have all benefited from his creativity. When Todd’s dream to play major league base-

ball didn’t happen, he fell back on another interest he developed as a teenager—drawing superheroes. He faced the same question faced

by all entrepreneurs: Could he make money pursuing his dream? He sent his sketches to prospective employers, and after 300 rejection letters Todd got a job freelancing for Marvel Comics. Working many hours for low pay, Todd made a name for himself and by 1990 was the highest-paid comic book artist in the industry.

Frustrated over creative differences and his desire to own the rights to his characters, Todd quit, took six other artists with him, and started his own company. He went from artist to entrepreneur overnight. While industry experts predicted he would last less than a year, Todd didn't even think about the future. *Spawn*, his first comic, sold 107 million copies.

Entrepreneurship rewards individuals willing to take risks. In Todd's case, the need to control his destiny drove his aspirations. His path is similar to that taken by many: receiving training at a large company, and then leaving when he decided he could provide a better product on his own.

Today's dynamic business environment has a tremendous effect on the success or failure of entrepreneurs like Todd McFarlane. Eco-

nomics plays a key role at the McFarlane Companies. Todd must protect the many intellectual properties the firm creates and licenses; laws are crucial to survival. The business uses technology to support and spark creativity in developing new products. The competitive environment drives quality at McFarlane, which produces high-quality products even if they cost more and thus gains an edge over competitors. The CEO uses the Web to interact with his key demographic, or, as he puts it, the "freaks" with long hair and cool tattoos. *Spawn.com* provides a place where fans can interact with each other and with the company. Finally, the global influence on business impacts all the other environments. Knowing he can't control the global environment, Todd focuses on managing what he can control and developing a culture where creativity thrives.

Todd's purchase of Mark McGwire's 70th home-run ball for \$3 million illustrates his willingness to take a risk and focus on what he controls. While many thought he was crazy, Todd saw an opportunity. He combined the ball with several other McGwire and Sosa balls to create the McFarlane Collection,

which was displayed in every major league stadium and led to enormous publicity. A portion of the proceeds was donated to the Lou Gehrig Foundation. Most significant, Todd began a relationship with professional sports that led to his obtaining the exclusive rights to nearly every professional sports-team toy license. Part of the deal with professional base ball teams has given Todd the chance to take batting practice in ball parks. As he says, "The best situation is when I can do something I want to do and it's good for business."

Questions

1. What traits do entrepreneurs like Todd McFarlane possess that distinguish them from other individuals? Do you think Todd has an internal or external locus of control?
2. What terminal and instrumental values would you say are important to Todd?
3. How does the organizational culture at McFarlane affect the creative process that leads to new products?

Chapter 3 Video Case: Enron

In August 2001, Enron vice president Sherron Watkins wrote an anonymous letter to her boss, Kenneth Lay, chairman of energy and telecommunications at the giant company. The memo warned that the company might "implode in a wave of accounting scandals." After meeting with Watkins, Lay called for Enron's attorneys at Vinson & Elkins to look into questionable partnership deals. In mid-October 2001, Enron announced a \$618 third-quarter loss and a write-

off of \$1.2 billion.¹ In December 2001, Enron—America's seventh-largest company in 2000—filed for Chapter 11 bankruptcy. Investment companies and individual investors lost billions; Enron employees lost jobs and retirement savings.

When a congressional subcommittee began looking into Enron's collapse in January 2002, it released Watkins's letter. Watkins subsequently testified that former CEO Jeffrey Skilling, who had left Enron in August 2001, misled Lay

about Enron's finances and that Skilling knew chief financial officer Andy Fastow had improperly profited from questionable partnerships set up to hide Enron's debt. At the hearings Skilling, who had sold \$66 million of his Enron stock during the previous three years while encouraging employees to continue buying company stock to fund their retirement, denied knowledge of any improprieties. Referring to the fact that Enron employees lost all their retirement

investment, Skilling said it was “very tough.”

The Justice Department and the Securities and Exchange Commission began lengthy criminal proceedings against Enron. Suits charged that Enron executives had committed fraud, inflating the value of the company's stock through false and misleading statements and the omission of material information. In 2004 a shocked public heard recordings of Enron traders' conversations that included cursing and derisive laughter about plans to cheat the public. By September 2004, some 30 individuals had been charged in various Justice Department and SEC cases.² Among them were Skilling and Lay, who each pleaded not guilty. Lay, who over five years had received around \$325 million in salary, bonuses, stock option gains, and stock sales, claimed he did not know what Fastow was doing.³ Several Enron executives, including Fastow, pleaded guilty to criminal conduct and became government witnesses in hopes of receiving reduced prison sentences.

The Enron demise also brought down Arthur Andersen, the 89-year-old, Chicago-based accounting firm that had been paid over \$1 million a week by Enron. With a team working inside the Enron building, Andersen had performed

the traditional accounting function of auditing Enron's financial statements but also served as Enron's internal auditor to help the company manage risk, a situation that critics have called a conflict of interest. At Enron's collapse, David Duncan, the Andersen auditor who had certified Enron's false financial reports, ordered massive record shredding and computer deleting. To limit damage, Andersen placed all blame on Duncan, fired him, and apologized in full-page newspaper ads for “errors in judgment . . . by Andersen personnel.” Such actions could not prevent legal action against Andersen. In the Enron hearings, documents from Enron's law firm Vinson & Elkins showed that Andersen auditors knew of Enron's questionable financial practices. Andersen was charged with obstructing the Security and Exchange Commission's investigation of Enron. Duncan himself pleaded guilty to obstruction of justice and became a key prosecution witness.⁴ In June 2002 Andersen was convicted; and in August 2002 the state of Texas revoked the firm's operating license, and a federal judge fined the company \$500,000 and sentenced it to five years' probation.⁵

Andersen—once an accounting giant with 85,000 employees and thousands of clients—did not sur-

vive. Several banking and securities firms that had deals with Enron suffered consequences in the form of fines, shareholder lawsuits, and criminal indictments of individuals. Meanwhile, Enron continued to sell assets as part of a reorganization plan to emerge from bankruptcy.

Sherron Watkins, who along with two other women executives was praised as a whistle-blower, was named Person of the Year in 2002 by *Time*. She resigned from Enron, wrote a book about her experiences, and began speaking to groups. Says Watkins, “I tell college students to be certain that ethics are at the top. Don't stay with a company that isn't ethical because something like an Enron could happen to you.”⁶

Questions

1. Which groups of stakeholders were harmed when Enron collapsed? Explain how each group was affected.
2. Which approach to social responsibility do you think Enron demonstrated? Which approach did Arthur Andersen demonstrate? Justify your choice for each company.
3. How does reputation affect the success of a service organization such as Arthur Andersen?

Chapter 4 Video Case: Cirque du Soleil

In 1984, Guy Laliberté left his home in Canada to make his way across Europe as a circus performer. There he and other artists entertained in the street. The troupe was called Cirque du Soleil—circus of the sun. It started with a simple dream: a group of young artists getting together to entertain audi-

ences, see the world, and have fun doing it.¹ Laliberté and company quickly found that their entertainment form without words—stilt-walking, juggling, music, and fire breathing—transcended all barriers of language and culture. Though he understood that an entertainer could bring the exotic to every cor-

ner of the world, Laliberté did not envision the scope to which his Cirque du Soleil would succeed. In 20-plus years of live performances, 44 million people have seen a Cirque show.² Despite a long-term decline in the circus industry, Cirque has increased revenue 22-fold over the last ten years.³ Today

Cirque performs five permanent shows—four in Las Vegas and one in Walt Disney World—and five traveling shows. Combined they gross about \$500 million annually.⁴ Growth plans include additional tours in Asia and permanent shows in New York, Tokyo, and London.⁵ In Interbrand's 2004 poll of brands with the greatest global impact, Cirque du Soleil ranks 22, ahead of McDonald's, Microsoft, and Disney.⁶

Cirque du Soleil is a family of more than 3,000 individuals—700 of whom are the shows' artists—from 40 different countries.⁷ Each of Cirque's employees is encouraged to contribute to the group. This input has resulted in rich, deep performances and expansion into alternative media outlets such as music, books, television, film, websites, and merchandising. The company's diversity assures that every show reflects many different cultural influences. Different markets will have an exotic experience at a Cirque show, regardless of which show is playing where. Cirque does target specific markets with products designed to engage a particular audience. Yet Cirque has little need to adapt its product to new markets; the product is already a blend of global influences. The result is a presentation of acrobatic arts and traditional, live circus with an almost indescribable freshness and beauty.

Cirque du Soleil's commitment to excellence and innovation transcends cultural differences and the

limits of many modern media. Its intense popularity has made Cirque both the global standard of live entertainment and the place for talented individuals from around the world to perfect their talents. The extent of the diversity, however, does pose a host of unique challenges. Every employee must be well-versed in various forms and styles. To foster cultural enrichment, Cirque purchases and shares a large collection of art with employees and gives them tickets to different events and shows.

The performers work in the most grueling and intimate situations, with their lives depending on one another. The astounding spectacles they achieve on stage result from hours of planning, practice, and painstaking attention to detail among artists from diverse cultures who speak 25 different languages. Sensitivity, compromise, and hunger for new experiences are prerequisites for success at Cirque. The organization has learned the art of sensitivity and compromise in its recruiting. Cirque du Soleil has had a presence in the Olympics for a decade. It works closely with coaches and teams to help athletes consider a career with Cirque *after* their competitive years are over, rather than luring talent away from countries that have made huge investments in athletes. This practice has given Cirque a huge advantage in the athletic community, a source of great talent from all over the globe.

Guy Laliberté has not forgotten his humble beginnings as a Canadian street performer. Now that Cirque du Soleil has achieved an international presence and incredible success—the group expects to be doing \$1 billion in annual gross revenue by 2007—it has chosen to help at-risk youth, especially street kids. Cirque allocates 1 percent of its revenues to outreach programs targeting youth in difficulty, regardless of location in the world.⁸ Laliberté understands that to be successful in a world market, one must be a committed and sensitive neighbor. Cirque's Montreal headquarters is the center of an urban revitalization project that the company sponsors. Community participation and outreach bring international goodwill and help Cirque du Soleil prevent many of the difficulties global brands often face when spanning culture.

Questions for Discussion

1. Why is Cirque du Soleil successful throughout the world? Why does the brand transcend cultural differences between countries?
2. In addition to culture, how do other forces in Cirque du Soleil's environment influence its decision making?
3. How does the changing global environment pose both opportunities and threats for managers at Cirque du Soleil?

Chapter 5 Video Case: *Columbia Space Shuttle Disaster and the Future of NASA*

Early on February 1, 2003, television viewers watched in disbelief and sadness as the space shuttle *Columbia*, returning from its

mission, seemed simply to break apart. Later, in a scathing report, investigators of the *Columbia* space shuttle disaster said that manage-

ment practices at NASA were as much to blame for the accident that killed seven astronauts as was the foam that broke away from the fuel

tank and hit the left wing during blast-off. The report basically concludes that NASA knew of problems with the foam insulation over a long period of time but never invested the time or energy needed to resolve the problem. Former astronaut and NBC analyst Sally Ride agrees with the findings. She notes that foam has been falling off the external tanks since the first shuttle launch and that it has fallen off on nearly every flight. Ride believes the foam problem was an accident waiting to happen, which of course it did. NASA had recognized the foam as a serious problem and tried to fix it, but, unfortunately, for some reason the foam didn't get as much attention as the many other problems NASA faced during the past decade.

Columbia is a sad reminder of the *Challenger* disaster 17 years earlier. In the case of *Challenger*, engineers suspected problems with O-rings but didn't fix them. It appears that NASA didn't learn from its mistakes with *Challenger*, and, more importantly, that a deeper problem exists: Safety concerns are not given top priority. According to Ride, while NASA officials do not suppress dissenting views, they do not encourage them. She notes that managers had the view that foam couldn't really cause a problem and they weren't looking to hear engineers tell them they were wrong. Echoes of *Challenger*? Ride thinks so. The further the investigation into *Columbia* progressed, the more

echoes were heard. The lessons learned in the years after 1986 seem to have been lost.

To ensure the vitality of the space program, NASA must change its culture. The can-do spirit must change to one of safety first; let's make sure we've done everything possible to guarantee safety. Changing the culture will take strong leadership and personal investment at all levels within NASA. Budgets and schedules can no longer be emphasized at the cost of safety. Processes must be put in place to make sure that anyone aware of a safety problem comes forward and is heard effectively up through the chain of management.

Safety is not the only issue putting pressure on the space program; NASA is also being scrutinized over its mission. For years NASA has been facing questions such as, What are we doing in space, and what is the payoff? Since the *Challenger* explosion, the goal has been to conduct scientific experiments and to construct the International Space Station, where people can live and work for months. But some experts say the science is just not that good. According to Professor Robert Park, none of the science from either the space shuttle or the space station has had a significant impact. While it may in fact be good research, Park thinks it simply is not very important. For instance, the shuttle and space station fly the same orbit John Glenn achieved in 1963;

much of what could be learned has already been learned.

Because of questions about its mission, NASA lives with constant budget pressure, which can threaten safety. The age of equipment is a concern, especially with the pressure applied to it. The idea that NASA has passed along useful products such as Teflon and Tang has also been questioned. According to Park, most of the products were developed independently; manufacturers found it good business to say their offerings had been developed in the space program.

With concerns over safety, budgets, and even its mission, what does the future hold for the space program? Only one thing is certain: The U.S. space program is in desperate need of a vision, one that was absent long before the *Columbia* disaster.

Questions

1. What seems to be the major problem facing NASA? What types of errors were made by managers? Was overconfidence a problem?
2. What must NASA accomplish to ensure the vitality of the space program? Do you think groupthink accounts for some of NASA's problems?
3. How could the steps in the decision-making process assist NASA in overcoming some of its problems?

Chapter 6 Video Case: JetBlue Airways

The day before JetBlue Airways made its first flight, founder and CEO David Neeleman gave an interview aboard a plane at New York's Kennedy International Air-

port. A smiling Neeleman exuded confidence and optimism as he explained what consumers could expect from the new low-cost national airline: A320 planes, the most tech-

nologically advanced in the world; friendly service; leather seats; larger overhead bins for more storage; and in each seat back, satellite television featuring 24 channels.

Industry newcomer JetBlue faced many challenges, however. Even history was against the upstart company; no airline founded since 1996 had survived; only a few founded in the last 25 years were still in business.

Even with the odds against him, Neeleman thought he had a plan to succeed. First, he brought experience. JetBlue is the third airline Neeleman has been involved with—he once worked for low-fare pioneer Southwest Airlines—so he understood the pitfalls in this business. Additionally, the airline started out with a significant amount of capital, about \$130 million, which enabled JetBlue to purchase new planes at the outset and order 82 more. Third, Neeleman's plan called for JetBlue to avoid some competition from the major airlines by flying in and out of airports that were not used or were underserved by major carriers. JetBlue's premier flights were out of Kennedy Airport to two cities, Buffalo and Fort Lauderdale. Neeleman's ambitious plan was to add one new city and one new plane about every month.

JetBlue's pricing was perhaps the linchpin of its strategy. For advanced-purchase seats, fares were set as low as \$79 from New York to Florida. With the most expensive fare set at \$159, JetBlue placed itself as a low-price carrier, but with premier service. One of Neeleman's aims was to overcome the perception that low fares mean poor-quality service. To "bring humanity back to air travel," as he put it, JetBlue would hire the best people and train them well.

JetBlue's entry into the market escalated the already intense competition in the airline industry. Within its first four years of operation, the airline was serving 25 cities, just as Neeleman had planned.¹ By 2004, revenues were approaching \$1 billion.² During this time the major airlines' revenues fell 10 percent, and they are not expected to ever fully rebound.³ With the majors (American, Delta, Continental, Northwest, United, and US Airways) struggling with high costs and dissatisfied customers, low-cost airlines like JetBlue and Southwest have been demonstrating how to make passengers happy while showing a profit. The difference has come down to costs. Southwest's operating costs per flight have been roughly half of those at major airlines, and JetBlue's costs at 6.4 cents a mile have been even lower than Southwest's 7.4 cents.⁴ When the economy was in high gear several years ago, the major airlines had a huge run-up in union wages. The low-fare airlines generally pay employees less and get more work from them. Because discount airlines also fly more direct flights, they don't have to wait for connections and can turn planes around faster; planes make money when they are in the air. Finally, JetBlue and other low-fare carriers can select the markets where they see the largest opportunities. As new companies, they don't have large national and international networks established.

Growth can bring problems, and all has not been perfect at JetBlue.

Stock prices reached a peak in October 2003 at \$47 a share and fell to \$23 in 2004.⁵ Some industry analysts say the airline expanded too fast, adding new routes and planes faster than demand. Also, JetBlue faces competition from other new low-fare airlines, such as AirTran, ATA, and Spirit, as well as those backed by the majors, such as Sony and Ted, started by Delta and United, respectively. Managing expansion has been the downfall of many firms in numerous industries. Southwest Airlines took 27 years to grow to 280 planes.⁶ David Neeleman has remained optimistic, seeing many new markets and plenty of opportunities for low-fare airlines and planning routes out of La Guardia, New York's other main airport.

Questions

1. What is the role of the CEO, such as David Neeleman, in developing plans and strategies? What traits are needed to be successful in this role?
2. What was Neeleman's plan for entering the airline market? Which factors were in his favor, and which were against him?
3. Why do growth companies like JetBlue often struggle with expansion? How could planning assist managers in overcoming the risks associated with rapid growth and expansion?

Chapter 7 Video Case: Now Who's Boss?

How can managers really find out what's involved in the jobs their employees do? Do the work

themselves, of course. That's what Jonathan Tisch, chairman and CEO of Loews Hotels, did at his Miami

Beach property. For days, he donned uniforms and worked in six entry-level jobs—bellman, breakfast

cook, room-service waiter, front-desk clerk, pool attendant, and housekeeper. Tisch was watched not only by his employees but also by viewers who saw *Now Who's Boss?* when the segment was aired on the Learning Channel.

For the role reversal, employees worked alongside Tisch or kept a close eye as he checked in guests, cooked omelets, delivered drinks poolside, or made beds with hospital corners and military precision. The CEO put himself and his ego on the line; he is shown fumbling, sweating, and struggling through various tasks. Afterward, the usual jobholders were asked to critique his performance. Tisch says he wanted honest assessments, and he got them, including a grade of C for his turn as housekeeper.

Working at hotel service jobs was not a totally new experience for Tisch, who grew up in the hospitality business. His family owned a chain of hotels along the East Coast, from New York to Miami. As a child, Tisch helped out in hotel kitchens during family vacations. At 16, he held a paying job as desk clerk at one of his family's hotels.¹ It had been a long time, however, since the CEO had worked in a service job.

The experience opened Tisch's eyes to the difficulty of the work and the amount of training and experience required to do it well. As a desk clerk, he lacked the computer skills needed to quickly register guests; he saw firsthand the demands of welcoming tired or cranky arrivals. In Miami's summer heat, he felt the discomfort of polyester uniforms. He spent an exhausting three hours cleaning a room instead of the typical half hour. The housekeepers laughed when Tisch recounted his troubles and applauded when he expressed his respect for them and his appreciation for the demands of their job—the toughest one, the CEO found. Respect for employees and rapport with them are two big benefits he derived. "People say, 'If the CEO is willing to clean toilets and make beds, then he must care about us.'"²

The job switching required hard work and a significant amount of executive time—a half day per job—but Tisch saw tremendous value in it. "I thought I had all the answers," he says, "but looking at all these positions with the eye of a CEO, I learned a lot."³ Tisch started a companywide "Now Who's Boss?"

day. Every year the managers and senior staff of each hotel take a day to work in a service job. Employee roundtables often follow so that Loews personnel can share and evaluate experiences. The communication helps everyone recognize what's required in the day-to-day running of a hotel.

The hotel business has changed in the 35 years Tisch has been involved; it is now very technical and highly competitive. But he says the nature of the hospitality industry has stayed the same for hundreds of years: "When you are in the hotel business, you have to create partnerships with employees and guests."⁴

Questions

1. Describe how jobs would be designed at a hotel such as Loews.
2. Describe the organizational structure of a Loews hotel.
3. According to the job characteristics model, how would you rate the jobs performed by hotel employees?

Chapter 8 Video Case: BP: Building a Global Brand

British Petroleum (BP) was a midsize international company before 1998. Then, over four years, the company doubled in size and expanded into new markets. A merger with Amoco gave BP an important position in the American market. BP then acquired Arco, another American firm, to gain a coast-to-coast presence in the United States. Acquiring the lubricant brand Castrol, the German

company Aral, and several other firms resulted in a strong presence in the European market. Growing from 55,000 employees to 117,000, BP emerged as one of the world's largest energy companies and faced the challenge of reinventing itself as a global corporation.

The merging of nine companies made BP a company with no common past, but its leaders recognized the need for a common

future. BP undertook a major initiative to rebrand itself so that everyone in the organization could identify with the large new company. The objective was to create a sense of belonging through a new set of values with which all employees could align and relate in their everyday dealings with customers and other stakeholders.

To create the new brand, BP consulted employees from all of its

component companies. Four core values were identified:

Performance—about meeting goals, including financial performance.

Innovation—about allowing your people to seek new solutions to new problems.

Progressive—relating to an attitude that constantly challenges the organization and recognizes diversity.

Green—representing the organization's responsibility to society and the environment (for example, searching for new types of fuels and engines).

BP looks at these four values as its corporate brand, what BP stands for, and how it operates. They influence the approach everyone at BP takes. These core values move beyond cultural differences and business environments throughout the world. Ways of doing business may differ, but the values remain the

same. For instance, the operating guidelines BP has established in Columbia are stricter than those required by the local and national legislatures. BP applies its core values even if doing so means taking a more difficult route.

Employees were crucial to the successful implementation of the new brand. A major challenge was to unify, excite, and motivate the entire organization. To get employees to understand and commit to the core values, BP made the brand a major part of a training process that occurs throughout employees' careers. In "brand modules," employees discuss with team leaders the core values and what they actually mean in their daily lives. Once employees internalize the firm's values, delivery across various cultures comes naturally.

After the new brand was developed, it had to be communicated externally. BP faced the challenge of changing consumers' negative view of the oil industry. One strategy was

to base marketing efforts on the core values to create a positive response in the minds of customers and to establish a new type of relationship with society. BP put one group in charge of worldwide communication to develop a consistent message to the public and at the same time be responsive to local needs.

Questions

1. Why was it important for BP to change its brand? What was the objective of the rebranding initiative?
2. What role did employees have in establishing the four core values? How does the set of values influence the behavior of BP employees?
3. What challenges did BP face in implementing the new brand? How did BP meet those challenges?

Chapter 9 Video Case: Working for the Best: The Container Store

The Container Store management hopes that customers will immediately notice two things: great products and happy employees. A perennial among the top five on lists of best companies, The Container Store twice has been selected by *Fortune* magazine as the number-one company to work for in the United States. According to chairman and co-founder Garrett Boone, this recognition results directly from hiring great people—one of the six foundation principles that constitute the company's culture. The key is for employees to provide great customer service *when* it is needed, whether it be helping a customer organize a garage or closet or

answering a simple question. Great service requires motivated employees who are empowered to exceed customer expectations.

How are employees at The Container Store motivated to provide great customer service? Managers have applied several theories of motivation to develop a culture in which jobs are interesting and employees are not afraid to take a chance. They are not afraid to fail. While Taylor and the scientific management proponents emphasized efficiency and proper programming, The Container Store takes a much more humanistic approach to motivating by recognizing a wide range of employee needs.

In the 1950s, psychologist Abra-

ham Maslow theorized that people are motivated to satisfy current needs in the categories of physiological, safety, social, esteem, and self-actualization. The categories form a hierarchy, with the most basic needs, physiological and safety, at the bottom. The higher-level needs—social, esteem, and self-actualization—are at the top of the hierarchy. The Container Store plays a role in meeting all these employee needs. Wages, among the highest in the industry, help individuals satisfy physiological needs and motivate employees to perform at higher levels of productivity. The environment helps people feel emotionally secure by stressing such values as integrity,

honesty, and open communication. Social needs are met by The Container Store's family atmosphere, where people feel they belong to a group. By recognizing employees both formally and informally when they do something extra special, the company helps employees meet the need for esteem. Finally, the highest-level need of self-actualization is met by encouraging employees to reach their highest potential. Many part-time employees become full-time employees; many of the managers began their careers as part-timers. The turnover at The Container Store provides some evidence that employees' needs are being met. The company averages about 15 to 20 percent in an industry where turnover is 90 to 100 percent annually.

The Container Store also seeks out managers who follow McGregor's (Chapter 2) Theory Y in their assumptions about employees. Theory Y assumes that workers are not lazy by nature and, when the

opportunity arises, will do what is best for the organization. Following this belief fosters a relaxed atmosphere and empowered workers. Employees are expected to think for themselves and are given the authority to make decisions without checking with a manager first.

Pride in the work itself is also obvious at The Container Store. Employees are cross-trained so that they understand everyone else's job, a practice that makes jobs more interesting and prepares employees to make decisions should the need arise. In effect, employees operate much like a store manager, capable of making decisions that generate better customer service.

The Container Store also emphasizes coaching and learning. Managers work with employees on a daily and weekly basis to help them develop skills, work on weaknesses, and enhance strengths. Victor Vroom's expectancy theory states that the amount of effort employees put in depends on their

expectations of the outcome. Similarly, equity theory deals with the question "If I do a good job, will it be worth it? What's fair?" When it comes to employee expectations and equity, the key point is that organizations communicate effectively. Kip Tendell, The Container Store's president and CEO, says that communication is the number-one factor when it comes to motivation. Open communication extends down to the team level, where peers are encouraged to share their knowledge with one another regardless of position.

Questions

1. Using Maslow's hierarchy of needs, explain how The Container Store satisfies the needs of its employees.
2. How are workers at The Container Store motivated?
3. Why don't managers at The Container Store use just one approach in motivating employees?

Chapter 10 Video Case: The Legacy of GE's Jack Welch

As General Electric's chairman, Jack Welch was one of the world's most powerful corporate leaders. He was also viewed as one of America's toughest executives and an icon to be admired. The now-retired Welch, his famous management style, and his accomplishments have been the subjects of books and university business classes.

Under Welch, from 1981 to 2001, GE became the world's most valuable company, with a market value of \$406 billion. Welch spurred that dramatic growth by performing management functions his own way. He chose not to follow the traditional strategy of sticking with

what a company knows but instead, accumulated diverse businesses. Originally a manufacturer of household appliances, lighting, and jet engines, GE bought NBC as well as companies offering medical products, financial services, and car leasing.

Welch restructured GE before restructuring became common among large corporations. Although his company was profitable, Welch sold some of GE's subsidiaries and reduced the payroll. Some 118,000 jobs—about one in four—were slashed. The deep cuts earned Welch the nickname "Neutron Jack," a moniker he is said to have detested. Welch endured the criticism

and continued his practice of identifying, keeping, and rewarding high-performing employees at General Electric.

Welch is known for dismantling GE's large bureaucracy and opening up corporate communication. Some have said that Welch listened as much as he talked and that he always spoke in a straightforward manner. He excelled at personal interaction and motivation and as the top executive was highly visible in his company. Welch visited and taught at GE's famous Management Development Institute in Crotonville, New York. His leadership style centered on having strong employees and managers

at all levels and empowering them to make decisions and engage in what he called “boundaryless thinking.”¹

Some people who worked with Welch have described the former chairman’s interaction as more aggressive than egalitarian or cooperative. Others have said that Welch’s often-used motivational technique was the fear factor: perform or hit the road. Welch determined in the early 1980s that to be at the top, GE could not fill management positions with deadwood—people who felt comfortable, secure, and protected from competition in their jobs within the depths of a large corporation. Welch thought it was better for individuals performing at the lowest levels to move on in other directions when they are young. During his tenure at GE, Welch selected the best people he could find and then trained and promoted them. Many who learned from him

took their leadership skills to other large firms. Some of Welch’s “lieutenants” head some of the world’s major corporations, such as Home Depot, TRW, 3M, and others.

Widely publicized and lauded, Welch’s leadership techniques also surface in noncorporate environments. The head of the Junior League of London, a nonprofit organization of volunteers offering social services, has employed Welch-style principles to motivate her group’s 400 members.

Of course, Jack Welch’s years at GE included not only stunning corporate accomplishments but also setbacks and controversies. A proposed merger with Honeywell was rejected by European Union regulators. The Environmental Protection Agency under the Bush administration ordered GE, at a cost of \$500 million, to clean up 40 miles of Hudson River bottom polluted by PCBs before the substances were

banned. After Welch’s exit from GE in September 2001, critics attacked his substantial benefit package, including an arrangement that provided more than \$2 million a year for an array of perks such as air transportation and personal services. Welch promptly agreed to give back \$2 million.

Questions

1. In what ways did Jack Welch perform the leadership function effectively?
2. Identify the type of skills—conceptual, human, or technical—that was most likely Jack Welch’s strong suit when he was GE’s top executive. Explain.
3. Would you like to work for a leader like Jack Welch? What would be the advantages? What would be the disadvantages?

Chapter 11 Video Case: Pike Place Fish

Pike Place Fish is located in Seattle’s historic, open-air Pike Place Market. People come from many parts of the world to see the fish mongers throwing fish and having fun and to buy high-quality seafood and have it shipped home. From a humble beginning as a small fish stand, Pike Place Fish has gained a big reputation. The change began when a young employee said, “Let’s be world famous,” and the owner responded, “Why not?”

John Yokoyama worked at Pike Place Fish when the owner offered to sell him the business in 1965. Only 25, Yokoyama was reluctant to buy the struggling market, but after much thought he decided to give it a try. Yokoyama knew nothing about

managing people, and his management style was that of a tyrant: You do what I tell you or else. Pike Place Fish did not do well, and Yokoyama was close to failing. That’s when Jim Bergquist entered the scene.

A consultant whose wife worked at the fish market, Bergquist approached Yokoyama with a proposition: Give me three months and I’ll improve your business, or else I’ll quit. They agreed. Then, when they were trying to decide their strategy, the young worker made his wild suggestion. At first the partners regarded the notion of becoming world famous as a joke, but the idea began to grow on them. They adopted the idea and added the words *world famous* to the com-

pany’s logo and had them printed on shipping boxes.

What does it mean to be world famous? That’s what Yokoyama, Bergquist, and their crew had to figure out. They decided it means making a difference in the lives of customers and others with whom they come into contact. “For us it means going beyond just providing outstanding service to people,” explains Yokoyama. “We’re out to discover how we can make their day. We’ve made a commitment to have our customers leave with the experience of having been served. They experience being . . . appreciated whether they buy fish or not.”¹

Providing such an experience for customers requires total commitment. At Pike Place Fish, there

are no jobs but, rather, positions available for those who make the team. You have to commit to the purpose—being world famous—or you won't even want to be on the team. New employees sometimes take three months to understand the distinction—*being* world famous rather than merely wanting to be or believing you are—and become productive team members.

A big change for John Yokoyama was sharing responsibility and power with workers. Yokoyama found that the best way to manage the type of team he needed was to stay out of employees' way and let them be creative and manage themselves. Inspirational manage-

ment is the preferred style. Pike Place Fish creates a context for personal growth and development. For instance, someone who wants to master the art of filleting fish will be coached to reach that goal. Anyone can be a coach, and everyone is allowed to coach others. The intention is for the coach to empower the other person to achieve. When coaching is needed, everyone has the responsibility to step up and contribute.

Pike Place Fish has earned its fame without advertising, except on its Web site.² The company's success, the team says, is the result of its vision and commitment to making a difference for people.

Questions

1. What does it mean at Pike Place Fish to be world famous?
2. What role do teams play in Pike Place Fish's quest to be world famous? Why does it take new employees time, in some cases three months, to become productive team members?
3. How does Pike Place Fish create the context for workers to reach their maximum potential? What role do managers play in creating and nurturing this atmosphere?

Chapter 12 Video Case: Patagonia

Yvon Chouinard began climbing as a 14-year-old member of the Southern California Falconry Club. At the time, the only available pitons (spikes used in mountain climbing) were made of soft iron, used once, and left in the rock. In 1957 Chouinard bought a used coal-fired forge to make reusable iron pitons; the word spread, and soon he was in business.¹ From climbing equipment to apparel, his company, Patagonia, has evolved into a highly successful private firm with annual revenues of \$250 million. Chouinard has kept it private so that he can continue to pursue his mission: earth first, profits second.²

According to CEO Michael Crooke, Patagonia is a very special company with a set of core values that is more than the bottom line. Because of the basic values, employees come to work every day with the attitude that they are making a difference. For each new hire, Patagonia receives 900 résumés. To understand the firm's success in sat-

isfying employees, one need only to look at a catalog. Not many companies place such significance on environmental and social issues. From the start, Yvon Chouinard advocated a purer, equipment-light approach to making climbing hardware in order to preserve the environment.³ The philosophy has continued. A recent catalog featured an essay entitled, "Do you need this product?" The message? If you don't need another shirt or jacket, don't buy it. Patagonia's management believes that this honest approach, while rare, creates loyal customers and dedicated employees.

To many environmentalists, corporations are the enemy. Patagonia takes a different approach. The company's goal is to make a difference; to do so, it must use its power to work from within the system. Patagonia is a successful company socially, environmentally, and financially. The success starts with great products and great people. Product quality and guarantees assure that

the products meet high expectations at any store no matter the location in the world.

In choosing employees, Patagonia looks for people passionate about an interest or cause. Over the years, many workers with similar causes and values have joined the company. The culture is based on commitment to environmental, moral, ethical, and philosophical causes. Patagonia employees derive true meaning from work, family, and health, rather than money and status. The goal is psychological success, achieved through a pro-team career.

Patagonia spends little on recruiting. The firm experiences very low turnover, about 4 percent annually. Each year, *Fortune* magazine rates the company as one of the best to work for. Why have workers found so much satisfaction with their jobs at Patagonia? Four reasons:

Let My People Surf The philosophy of Yvon Chouinard, not only an

accomplished climber but also a passionate surfer, is that you have to surf when the surf's up. At Patagonia, workers set their own schedules; when they need to work, they get their jobs finished. To develop great products, you need to be users of the products. You can't develop great surfboards if you don't surf.

Enviro Internships After employees have completed a year, the company pays up to 60 days' salary for each individual to intern for an environmental group. The only requirement is that employees present a slide show when they return. Some employees have left Patagonia after the internships to become full-time activists. That's fine with the firm. Patagonia recently joined

with several other apparel companies and six leading anti-sweatshop groups to devise a single set of labor standards with a common factory inspection system.⁴

Child Development Center Started in 1985, the childcare facility is one of the first of its kind and an integral component of the company. Children are part of the campus all day, every day. The connection between work and family increases job satisfaction. Knowing their children are being well cared for onsite helps employees become fully committed.

One Percent for the Planet In 1985, Patagonia started an "earth tax" and donates one percent of sales to grassroots environmental activists worldwide. Each group has its own budget for local activism.

Patagonia employees serve on grant committees that fund proposals. Because of employee involvement, this program also contributes to worker satisfaction.

Questions for Discussion

1. What core values are important at Patagonia? How do these values play an important role in recruiting and retaining top employees?
2. Why is Patagonia ranked annually as one of the best companies to work for?
3. Why are people a critical component of Patagonia's success? How do employees help the firm gain a competitive advantage?

Chapter 13 Video Case: Louisville Slugger (Hillerich & Bradsby)

What do Babe Ruth's 60th home run, Joe Di Maggio's 56-game hitting streak, Ted Williams' .406 season, and Hank Aaron's record-breaking 715th home run have in common? They all were accomplished with Louisville Slugger bats manufactured on the Ohio River at Hillerich & Bradsby (H&B).¹ Best known for its bats—its wooden bats claim 60 percent of the major league market—H&B, based in Louisville, Kentucky, also manufactures a variety of baseball, golf, and hockey equipment for amateur and professional athletes.

The company was founded in 1857 as J.F. Hillerich & Son to manufacture butter churns. It entered the baseball market when one of Hillerich's sons, Bud, promised a star player he could make a bat for him. H&B began producing aluminum bats in 1928 and today relies on the wooden and aluminum bat

business for nearly three-quarters of its annual revenues.

The company remains family-run; John Hillerich IV, the fourth-generation CEO, took over the private company from his father. He feels the pressure heading a successful company that is over 120 years old, as competition in the industry has intensified like never before. The Louisville Slugger bat now competes with bats made by a host of other sources, ranging from carpenters to Amish craftspeople. To gain an advantage, H&B looked at its internal system in order to streamline operations. The company needed to address everything from order entry problems to production deficiencies to returns. The overview led to discussion of a new system to handle the flow of information.

H&B had a big decision to make: It could either reconfigure its information system or start over with a

new system designed to streamline the information flow in support of the sales operation and supply change management, as well as accounting, finance, and marketing. Management realized it needed a new system to improve the company's dismal shipping record; about 40 percent of its orders were being shipped on time. The managers opted for the enterprise resource planning (ERP) system, designed to simplify all processes by storing all information in one common database and automatically updating the information in every stage of production.

Implementation of the new ERP system usually takes years, and the transition from the old system to the new one is difficult. Since the ERP system uses real-time information, the production department manufactures only the inventory that the sales department has requested,

so the shipping department has the proper amount of inventory to send to customers. The benefits of ERP are bottom-line savings for the company and improved morale as frustration from repetitive tasks and missing information dissipates. H&B managers thought that the cost of implementing the new system was worth the potential savings. Communication between production and sales had been inefficient, as well as that with management. Getting an answer to one simple question could take a week.

The first step in streamlining production was to identify problems and devise the needs of the new ERP system. Then, the German company SAP was chosen to provide the software. With the SAP

system, a common server holds all the company's information. Every personal computer (PC) is connected to the server. Once data are entered, they are stored in the server, where everyone can access the data from a PC.

During the 18-month configuration process, morale sagged as long-time employees struggled to change the way they worked. Some employees left during training classes, stress levels temporarily increased, and some production processes failed. H&B managers thought about halting the new system, but after struggling through implementation, the company began seeing benefits; it took five years to see quantifiable results. Now the company ships 85 percent of its or-

ders on time and complete, compared to 40 percent before the SAP system. Top customers surveyed rate H&B in the 90 to 95 percent satisfaction category.

Questions

1. What role do information systems play at H&B? What were the trade-offs between reconfiguring the old information system and designing a new one?
2. Why was the transition to the new system difficult? What can managers do to make this type of transition go more smoothly?
3. What were some of the benefits of the new system?

Chapter 14 Video Case: Starbucks: Building Relationships with Coffee Growers

As the world's largest supplier of premium-based coffee, Starbucks goes to great lengths to satisfy its customers. Since the company started in 1971, it has grown to nearly 6,000 outlets in 30 countries, with sales in excess of \$3.5 billion. A key to Starbucks' success is the relationship the firm has established with coffee growers.

Starbucks depends on the coffee bean for its success. Coffee is grown in 70 tropical nations, and quality varies tremendously from region to region. Starbucks buys a special grade of coffee—one grown at high altitudes—that is very dense. This density or compaction of flavors creates specialty coffee. The specialty-coffee industry has grown tremendously but still accounts for only 10 percent of world-wide coffee purchases.

During the past five years, the supply of coffee produced has

exceeded demand. As a result, the price has fallen below the break-even point for most producers, and small producers find that they can't survive in this environment. Starbucks realizes it needs quality growers so that quality coffee will be available in years to come.

To ensure a steady supply of specialty-coffee beans, Starbucks invests heavily in its relationships with suppliers. Starbucks buys primarily from small farmers, teaching them how to produce specialty coffee. Starbucks also pays above market price for coffee, thereby enabling small farmers to stay in business. Prices are set for a year, so farmers lock in a profit.

To stabilize prices, Starbucks has begun to negotiate long-term contracts with growers. As a result, Starbucks is guaranteed a regular supply of products and growers are assured of future sales at pre-

dictable prices. Farmers can then invest in their business to ensure supply in the years ahead.

Starbucks has recently partnered with Ecologic Enterprise Ventures and Conservation International, two nonprofit organizations, to provide affordable credit to coffee farmers in Latin America. This works like a bridge loan to farmers who are ecologically friendly so that they can pay their pickers until the crop is harvested. As with the long-term contracts, this arrangement helps to ensure that growers will be around for years to come.

Starbucks has also begun to sell Fair Trade Coffee. To be certified by Fair Trade Labeling (FLO) Organizations International, coffee producers must belong to democratically run cooperatives or associations and must implement crop management and environmental protection plans. Price incentives

are used to encourage producers to work toward organic production. In return, they are guaranteed a fair price, long-term relationships with importers, and credit. Starbucks offers Fair Trade Coffee in its retail stores, and the product is coffee of the day at least once a month.

Starbucks has also partnered with Conservation International to encourage environmentally friendly coffee-growing practices in a reserve

in Mexico. Trees are no longer cut down to plant coffee trees. The result is a smooth, mellow coffee grown in shade, the very popular Shade Grown Mexico.

Questions

1. Why are relationships with growers critical to Starbucks' success in satisfying its customers?

2. What strategies are used by Starbucks to improve relationships with suppliers? How could these strategies lead to a competitive advantage?
3. Why is quality critical in the specialty-coffee industry? How do relationships with both suppliers and other organizations influence quality at Starbucks?

Appendix: Management Careers Video Case eBay

eBay changed merchant Karen Young's life. Young, a housewife, was selling used computer parts on eBay and spending a lot of money wrapping and packaging them when the light went on in her head. Now known as the "bubble wrap lady," Young sold about a half million dollars in shipping supplies in 2004. She is one of the millions of registered users of the huge online auction, where buyers and sellers can bargain over a huge variety of goods ranging from rare valuables to junk. According to Young, "If you can't find it on eBay, you can't find it." Like many eBay users, she found a new career through the auction site.

Many eBay users consider themselves part of a big, happy family. As many as 4,400 people have gathered in Anaheim, California, at eBay Live for a chance to meet other vendors face-to-face and link a user name with an actual person. Some discontentment has arisen, though, among smaller sellers concerned that large companies have set up shop on eBay. Adam Cohen, who wrote the book, *The Perfect Store*, notes the difficulty eBay faces in achieving a delicate balance: attracting and satisfying investors by bringing in big

sellers and high-priced items, while at the same time catering to small individual sellers—the moms and pops. CEO Meg Whitman understands that keeping people like the bubble wrap lady happy will keep her business prospering.

Whitman, who says she learned from her mother to never fear the future, left a terrific job and moved her family across the country to take over at the San Jose, California-based eBay. A graduate of Princeton University and Harvard Business School, she moved up the ranks at several blue chip companies such as FTD, Procter & Gamble, and the Walt Disney Company, then jumped into the upstart world of online business with little knowledge of the Internet. In two years the workforce grew from 5 to 800. eBay stock rose 2,400 percent since going public. The company has about eight million customers. The number of registered users has grown sharply; in 2005 their ranks swelled to 157.3 million, a 38-percent increase in one year.¹ In that same period 64.4 million people bid, bought, or listed an item. Each day, more than 3.3 million items go up for sale.

The mission at eBay, according to Whitman, is to create a global

online marketplace where the next-door neighbor's chances of success are equal to those of a large corporation.² To accomplish this, almost anything can be sold on eBay. (There are limits to eBay offerings; the auction site won't allow trade in body parts, for example, or a person's soul.) Sellers and buyers can be almost anywhere. While the company had no international operations five years ago, it now has 31 sites throughout the world. Management expected eBay's international trading revenue to surpass domestic revenue at the end of 2005. Approximately half of eBay's registered users are outside the United States.³

The future looks bright for eBay, which claimed \$1.1 billion in revenue in July 2005.⁴ Looking for growth, the company has acquired businesses to diversify its revenue from auctions by adding fixed-price listings such as classified ads and rental-property listings.⁵ Much of eBay's success has been credited to CEO Whitman, who led the transformation from a little Internet auction site into a vast global marketplace that dominates its category. Board member Robert Kogle says that Whitman is into winning competitively and is one of the best

strategists he has ever met. To handle eBay's rapid growth, she has restructured the organization several times, which she says keeps people excited and gives them new opportunities. Motivation comes from the eBay mission and empowerment. "We give people a chance to settle in," she says, "and then we make sure that they are well-managed, that they are focused on high-impact projects, and that they understand the results they are going to be accountable for."⁶

The company's future may not include Whitman for long. In 2005 she was the top outside candidate for the CEO job at Disney, then withdrew her name, a move many con-

sidered a plus for eBay. "She loves this company and the employees," says eBay spokesman Henry Gomez.⁷ Industry experts think the visibility of the Disney search will make her an even more attractive candidate for other CEO jobs. Whitman herself has said that 10 years is the longest any CEO should remain at a company; companies need a fresh perspective and an energized leader to tackle corporate challenges.⁸ After seven years as CEO, Whitman has begun grooming several senior managers who may eventually be chosen to replace her. Three senior executives have rotated jobs, a situation seen as Whitman's way to get each manager to

learn about other corporate units and to share expertise.⁹ Other executives have joined eBay in management and technical positions as Whitman continues to populate the company with strong managers.

Questions for Discussion

1. What types of careers are possible through eBay?
2. Why would someone like Karen Young want to develop a career based on using eBay?
3. Why don't successful leaders like Meg Whitman stay with one company for their entire careers?

Glossary

A

ACHIEVEMENT ORIENTATION A worldview that values assertiveness, performance, success, competition, and results.

ADMINISTRATIVE MANAGEMENT The study of how to create an organizational structure that leads to high efficiency and effectiveness.

ADMINISTRATIVE MODEL An approach to decision making that explains why decision making is inherently uncertain and risky and why managers usually make satisfactory rather than optimum decisions.

AGREEABLENESS The tendency to get along well with other people.

AMBIGUOUS INFORMATION Information that can be interpreted in multiple and often conflicting ways.

APPLICATIONS SOFTWARE Software designed for a specific task or use.

ARTIFICIAL INTELLIGENCE Behavior performed by a machine that would be called intelligent if performed by a human being.

ATTITUDE A collection of feelings and beliefs.

ATTRACTION-SELECTION-ATTRITION FRAMEWORK A model that explains how personality may influence organizational culture.

AUTHORITY The power to hold people accountable for their actions and to make decisions concerning the use of organizational resources.

B

BARRIERS TO ENTRY Factors that make it difficult and costly for an

organization to enter a particular task environment or industry.

BEHAVIORAL MANAGEMENT The study of how managers should behave to motivate employees and encourage them to perform at high levels and be committed to the achievement of organizational goals.

BENCHMARKING Comparing performance on specific dimensions with the performance of high-performing organizations.

BIAS The systematic tendency to use information about others in ways that result in inaccurate perceptions.

BOTTOM-UP CHANGE Change that is implemented gradually and involves managers and employees at all levels of an organization.

BOUNDARY SPANNING Interacting with individuals and groups outside the organization to obtain valuable information from the task and general environments.

BOUNDARYLESS CARRIER A career that is not attached to or bound to a single organization and consists of a variety of work experiences in multiple organizations.

BOUNDARYLESS ORGANIZATION An organization whose members are linked by computers, faxes, computer-aided design systems, and video teleconferencing and who rarely, if ever, see one another face-to-face.

BOUNDED RATIONALITY Cognitive limitations that constrain one's ability to interpret, process, and act on information.

BRAND LOYALTY Customers' preference for the products of organizations currently existing in the task environment.

BUREAUCRACY A formal system of organization and administration designed to ensure efficiency and effectiveness.

BUREAUCRATIC CONTROL Control of behavior by means of a comprehensive system of rules and standard operating procedures.

BUSINESS-LEVEL PLAN Divisional managers' decisions pertaining to divisions' long-term goals, overall strategy, and structure.

BUSINESS-LEVEL STRATEGY A plan that indicates how a division intends to compete against its rivals in an industry.

BUSINESS TO BUSINESS (B2B) NETWORK A group of organizations that join together and use IT to link themselves to potential global suppliers to increase efficiency and effectiveness.

C

CAFETERIA BENEFIT PLAN A plan from which employees can choose the benefits that they want.

CENTRALIZATION The concentration of authority at the top of the management hierarchy.

CHARISMATIC LEADER An enthusiastic, self-confident leader able to clearly communicate his or her vision of how good things could be.

CLAN CONTROL The control exerted on individuals and groups in an organization by shared values, norms, standards for behavior, and expectations.

CLASSICAL DECISION-MAKING MODEL A prescriptive approach to decision making based on the assumption that the decision maker can identify and evaluate all possible alternatives and

their consequences and rationally choose the most appropriate course of action.

CLOSED SYSTEM A system that is self-contained and thus not affected by changes occurring in its external environment.

COERCIVE POWER The ability of a manager to punish others.

COLLECTIVE BARGAINING Negotiation between labor unions and managers to resolve conflicts and disputes about issues such as working hours, wages, benefits, working conditions, and job security.

COLLECTIVISM A worldview that values subordination of the individual to the goals of the group and adherence to the principle that people should be judged by their contribution to the group.

COMMAND ECONOMY An economic system in which the government owns all businesses and specifies which and how many goods and services are produced and the prices at which they are sold.

COMMAND GROUP A group composed of subordinates who report to the same supervisor; also called a *department* or *unit*.

COMMUNICATION The sharing of information between two or more individuals or groups to reach a common understanding.

COMMUNICATION NETWORKS The pathways along which information flows in groups and teams and throughout the organization.

COMPETITIVE ADVANTAGE The ability of one organization to outperform other organizations because it produces desired goods or services more efficiently and effectively than they do.

COMPETITORS Organizations that produce goods and services that are similar to a particular organization's goods and services.

CONCEPTUAL SKILLS The ability to analyze and diagnose a situation and to distinguish between cause and effect.

CONCURRENT CONTROL Control that gives managers immediate feedback on how efficiently inputs are being transformed into outputs so that managers can correct problems as they arise.

CONCURRENT ENGINEERING The simultaneous design of the product and of the process for manufacturing the product.

CONSCIENTIOUSNESS The tendency to be careful, scrupulous, and persevering.

CONSIDERATION Behavior indicating that a manager trusts, respects, and cares about subordinates.

CONTINGENCY MODEL OF LEADERSHIP An approach that acknowledges that the quality of leadership depends on—is contingent on—the situation or context within which leadership occurs.

CONTINUOUS-PROCESS TECHNOLOGY Technology that is almost totally mechanized and is based on the use of automated machines working in sequence and controlled through computers from a central monitoring station.

CONTRACT BOOK A written agreement that details product development factors such as responsibilities, resource commitments, budgets, time lines, and development milestones.

CONTROLLING Evaluating how well an organization is achieving its goals and taking action to maintain or improve performance; one of the four principal functions of management.

CONTROL SYSTEMS Formal target-setting, monitoring, evaluation, and feedback systems that provide managers with information about how well the organization's strategy and structure are working.

CORE MEMBERS The members of a team who bear primary responsibility for the success of a project and who stay with a project from inception to completion.

CORPORATE-LEVEL PLAN Top management's decisions pertaining to the organization's mission, overall strategy, and structure.

CORPORATE-LEVEL STRATEGY A plan that indicates in which industries and national markets an organization intends to compete.

CREATIVITY A decision maker's ability to discover original and novel ideas that lead to feasible alternative courses of action.

CROSS-FUNCTIONAL TEAM A group of managers from different departments brought together to perform organizational tasks.

CULTURE SHOCK The feelings of surprise and disorientation that people experience when they do not understand the values, folkways, and mores that guide behavior in a culture.

CUSTOMERS Individuals and groups that buy the goods and services that an organization produces.

D

DATA Raw, unsummarized, and unanalyzed facts.

DECISION MAKING The process by which managers respond to opportunities and threats by analyzing options and making determinations about specific organizational goals and courses of action.

DECISION SUPPORT SYSTEM An interactive computer-based management information system with model-building capability that managers can use when they must make nonroutine decisions.

DECODING Interpreting and trying to make sense of a message.

DELPHI TECHNIQUE A decision-making technique in which group members do not meet face-to-face but respond in writing to questions posed by the group leader.

DEMOGRAPHIC FORCES Outcomes of changes in, or changing attitudes toward, the characteristics of a population, such as age, gender, ethnic origin, race, sexual orientation, and social class.

DEPARTMENT A group of people who work together and possess similar skills or use the same knowledge, tools, or techniques to perform their jobs.

DEVELOPMENT Building the knowledge and skills of organizational members so that they will be prepared to take on new responsibilities and challenges.

DEVELOPMENTAL CONSIDERATION

Behavior a leader engages in to support and encourage followers and help them develop and grow on the job.

DEVIL'S ADVOCACY Critical analysis of a preferred alternative, made in response to challenges raised by a group member who, playing the role of devil's advocate, defends unpopular or opposing alternatives for the sake of argument.

DIFFERENTIATION STRATEGY

Distinguishing an organization's products from the products of competitors in dimensions such as product design, quality, or after-sales service.

DISCIPLINE Obedience, energy, application, and other outward marks of respect for a superior's authority.

DISTRIBUTIVE JUSTICE A moral principle calling for the distribution of pay raises, promotions, and other organizational resources to be based on meaningful contributions that individuals have made and not on personal characteristics over which they have no control.

DISTRIBUTIVE NEGOTIATION

Adversarial negotiation in which the parties in conflict compete to win the most resources while conceding as little as possible.

DISTRIBUTORS Organizations that help other organizations sell their goods or services to customers.

DIVERSIFICATION Expanding operations into a new business or industry and producing new goods or services.

DIVERSITY Differences among people due to age, gender, race, ethnicity,

religion, sexual orientation, socioeconomic background, and capabilities/disabilities.

DIVISION A business unit that has its own set of managers and functions or departments and competes in a distinct industry.

DIVISIONAL MANAGERS Managers who control the various divisions of an organization.

DIVISIONAL STRUCTURE An organizational structure composed of separate business units within which are the functions that work together to produce a specific product for a specific customer.

DIVISION OF LABOR Splitting the work to be performed into particular tasks and assigning tasks to individual workers.

E

ECONOMIC FORCES Interest rates, inflation, unemployment, economic growth, and other factors that affect the general health and well-being of a nation or world region.

ECONOMIES OF SCALE Cost advantages associated with large operations.

EFFECTIVENESS A measure of the appropriateness of the goals an organization is pursuing and of the degree to which the organization achieves those goals.

EFFICIENCY A measure of how well or productively resources are used to achieve a goal.

EMOTIONAL INTELLIGENCE The ability to understand and manage one's own moods and emotions and the moods and emotions of other people.

EMOTIONS Intense, relatively short-lived feelings.

EMPLOYEE STOCK OPTION A financial instrument that entitles the bearer to buy shares of an organization's stock at a certain price during a certain period of time or under certain conditions.

EMPOWERMENT Expanding employees' tasks and responsibilities.

ENCODING Translating a message into understandable symbols or language.

ENTREPRENEUR An individual who notices opportunities and takes responsibility for mobilizing the resources necessary to produce new and improved goods and services.

ENTREPRENEURSHIP The mobilization of resources to take advantage of an opportunity to provide customers with new or improved goods and services.

ENTROPY The tendency of a system to lose its ability to control itself and thus to dissolve and disintegrate.

ENVIRONMENTAL CHANGE The degree to which forces in the task and general environments change and evolve over time.

EQUAL EMPLOYMENT OPPORTUNITY

The equal right of all citizens to the opportunity to obtain employment regardless of their gender, age, race, country of origin, religion, or disabilities.

EQUITY The justice, impartiality, and fairness to which all organizational members are entitled.

EQUITY THEORY A theory of motivation that focuses on people's perceptions of the fairness of their work outcomes relative to their work inputs.

ESPRIT DE CORPS Shared feelings of comradeship, enthusiasm, or devotion to a common cause among members of a group.

ETHICAL DECISION A decision that reasonable or typical stakeholders would find acceptable because it aids stakeholders, the organization, or society.

ETHICAL DILEMMA The quandary people find themselves in when they have to decide if they should act in a way that might help another person or group even though doing so might go against their own self-interest.

ETHICS The inner guiding moral principles, values, and beliefs that

people use to analyze or interpret a situation and then decide what is the “right” or appropriate way to behave.

ETHICS OMBUDSMAN An ethics officer who monitors an organization’s practices and procedures to be sure they are ethical.

EXECUTIVE SUPPORT SYSTEM A sophisticated version of a decision support system that is designed to meet the needs of top managers.

EXPATRIATE MANAGERS Managers who go abroad to work for a global organization.

EXPECTANCY In expectancy theory, a perception about the extent to which effort results in a certain level of performance.

EXPECTANCY THEORY The theory that motivation will be high when workers believe that high levels of effort lead to high performance and that high performance leads to the attainment of desired outcomes.

EXPERT POWER Power that is based in the special knowledge, skills, and expertise that a leader possesses.

EXPERT SYSTEM A management information system that employs human knowledge captured in a computer to solve problems that ordinarily require human expertise.

EXPORTING Making products at home and selling them abroad.

EXTERNAL LOCUS OF CONTROL The tendency to locate responsibility for one’s fate within outside forces and to believe that one’s own behavior has little impact on outcomes.

EXTINCTION Curtailing the performance of dysfunctional behaviors by eliminating whatever is reinforcing them.

EXTRAVERSION The tendency to experience positive emotions and moods and to feel good about oneself and the rest of the world.

EXTRINSICALLY MOTIVATED BEHAVIOR Behavior that is performed to acquire

material or social rewards or to avoid punishment.

F

FACILITIES LAYOUT The operations management technique whose goal is to design the machine-worker interface to increase production system efficiency.

FEEDBACK CONTROL Control that gives managers information about customers’ reactions to goods and services so that corrective action can be taken if necessary.

FEEDFORWARD CONTROL Control that allows managers to anticipate problems before they arise.

FILTERING Withholding part of a message out of the mistaken belief that the receiver does not need or will not want the information.

FIRST-LINE MANAGER A manager who is responsible for the daily supervision of nonmanagerial employees.

FLEXIBLE MANUFACTURING Operations management techniques that attempt to reduce the setup costs associated with a production system.

FOCUSED DIFFERENTIATION STRATEGY Serving only one segment of the overall market and trying to be the most differentiated organization serving that segment.

FOCUSED LOW-COST STRATEGY Serving only one segment of the overall market and being the lowest-cost organization serving that segment.

FOLKWAYS The routine social conventions of everyday life.

FORMAL APPRAISAL An appraisal conducted at a set time during the year and based on performance dimensions and measures that were specified in advance.

FORMAL GROUP A group that managers establish to achieve organizational goals.

FRANCHISING Selling to a foreign organization the rights to use a brand

name and operating know-how in return for a lump-sum payment and a share of the profits.

FREE-MARKET ECONOMY An economic system in which private enterprise controls production and the interaction of supply and demand determines which and how many goods and services are produced and how much consumers pay for them.

FREE-TRADE DOCTRINE The idea that if each country specializes in the production of the goods and services that it can produce most efficiently, this will make the best use of global resources.

FRIENDSHIP GROUP An informal group composed of employees who enjoy each other’s company and socialize with each other.

FUNCTION A unit or department in which people have the same skills or use the same resources to perform their jobs.

FUNCTIONAL-LEVEL PLAN Functional managers’ decisions pertaining to the goals that they propose to pursue to help the division attain its business-level goals.

FUNCTIONAL-LEVEL STRATEGY A plan that indicates how a function intends to achieve its goals.

FUNCTIONAL MANAGERS Managers who supervise the various functions, such as manufacturing, accounting, and sales, within a division.

FUNCTIONAL STRUCTURE An organizational structure composed of all the departments that an organization requires to produce its goods or services.

G

GATEKEEPING Deciding what information to allow into the organization and what information to keep out.

GENDER SCHEMAS Preconceived beliefs or ideas about the nature of men and women, their traits, attitudes, behaviors, and preferences.

GENERAL ENVIRONMENT The wide-ranging economic, technological,

sociocultural, demographic, political and legal, and global forces that affect an organization and its task environment.

GEOGRAPHIC STRUCTURE An organizational structure in which each region of a country or area of the world is served by a self-contained division.

GLASS CEILING A metaphor alluding to the invisible barriers that prevent minorities and women from being promoted to top corporate positions.

GLOBAL FORCES Outcomes of changes in international relationships, changes in nations' economic, political, and legal systems, and changes in technology, such as falling trade barriers, the growth of representative democracies, and reliable and instantaneous communication.

GLOBAL ORGANIZATION An organization that operates and competes in more than one country.

GLOBAL OUTSOURCING The purchase of inputs from foreign suppliers, or the production of inputs abroad, to lower production costs and improve product quality or design.

GLOBAL STRATEGY Selling the same standardized product and using the same basic marketing approach in each national market.

GOAL-SETTING THEORY A theory that focuses on identifying the types of goals that are most effective in producing high levels of motivation and performance and explaining why goals have these effects.

GRAPEVINE An informal communication network along which unofficial information flows.

GROUP Two or more people who interact with each other to accomplish certain goals or meet certain needs.

GROUP COHESIVENESS The degree to which members are attracted or loyal to a group.

GROUP DECISION SUPPORT SYSTEM An executive support system that links top

managers so that they can function as a team.

GROUP NORMS Shared guidelines or rules for behavior that most group members follow.

GROUP ROLE A set of behaviors and tasks that a member of a group is expected to perform because of his or her position in the group.

GROUPTHINK A pattern of faulty and biased decision making that occurs in groups whose members strive for agreement among themselves at the expense of accurately assessing information relevant to a decision.

GROUPWARE Computer software that enables members of groups and teams to share information with each other.

H

HAWTHORNE EFFECT The finding that a manager's behavior or leadership approach can affect workers' level of performance.

HERZBERG'S MOTIVATOR-HYGIENE THEORY A need theory that distinguishes between motivator needs (related to the nature of the work itself) and hygiene needs (related to the physical and psychological context in which the work is performed) and proposes that motivator needs must be met for motivation and job satisfaction to be high.

HIERARCHY OF AUTHORITY An organization's chain of command, specifying the relative authority of each manager.

HOSTILE WORK ENVIRONMENT SEXUAL HARASSMENT Telling lewd jokes, displaying pornography, making sexually oriented remarks about someone's personal appearance, and other sex-related actions that make the work environment unpleasant.

HUMAN RELATIONS MOVEMENT Advocates of the idea that supervisors receive behavioral training to manage subordinates in ways that elicit their cooperation and increase their productivity.

HUMAN RESOURCE MANAGEMENT

Activities that managers engage in to attract and retain employees and to ensure that they perform at a high level and contribute to the accomplishment of organizational goals.

HUMAN RESOURCE PLANNING Activities that managers engage in to forecast their current and future needs for human resources.

HUMAN SKILLS The ability to understand, alter, lead, and control the behavior of other individuals and groups.

HYBRID STRUCTURE The structure of a large organization that has many divisions and simultaneously uses many different organizational structures.

I

IMPORTING Selling at home products that are made abroad.

INCREMENTAL PRODUCT INNOVATIONS Products that result from incremental technological changes.

INCREMENTAL TECHNOLOGICAL CHANGE Change that refines existing technology and leads to gradual improvements or refinements in products over time.

INDIVIDUAL ETHICS Personal values and attitudes that govern how individuals interact with other people.

INDIVIDUALISM A worldview that values individual freedom and self-expression and adherence to the principle that people should be judged by their individual achievements rather than by their social background.

INDUSTRY LIFE CYCLE The changes that take place in an industry as it goes through the stages of birth, growth, shakeout, maturity, and decline.

INEQUITY Lack of fairness.

INFORMAL APPRAISAL An unscheduled appraisal of ongoing progress and areas for improvement.

INFORMAL GROUP A group that managers or nonmanagerial employees form to help achieve their own goals or meet their own needs.

INFORMAL ORGANIZATION The system of behavioral rules and norms that emerge in a group.

INFORMATION Data that is organized in a meaningful fashion.

INFORMATION DISTORTION Changes in meaning that occur as information passes through a series of senders and receivers.

INFORMATION OVERLOAD A superabundance of information that increases the likelihood that important information is ignored or overlooked and tangential information receives attention.

INFORMATION RICHNESS The amount of information that a communication medium can carry and the extent to which the medium enables the sender and receiver to reach a common understanding.

INFORMATION SYSTEM A system for acquiring, organizing, storing, manipulating, and transmitting information.

INFORMATION TECHNOLOGY The means by which information is acquired, organized, stored, manipulated, and transmitted.

INITIATING STRUCTURE BEHAVIOR

Behavior that managers engage in to ensure that work gets done, subordinates perform their jobs acceptably, and the organization is efficient and effective.

INITIATIVE The ability to act on one's own, without direction from a superior.

INNOVATION The implementation of creative ideas in an organization.

INPUT Anything a person contributes to his or her job or organization.

INSTRUMENTALITY In expectancy theory, a perception about the extent to which performance results in the attainment of outcomes.

INSTRUMENTAL VALUE A mode of conduct that an individual seeks to follow.

INTEGRATING MECHANISMS Organizing tools that managers can use to increase communication and coordination among functions and divisions.

INTEGRATIVE BARGAINING Cooperative negotiation in which the parties in conflict work together to achieve a resolution that is good for them both.

INTELLECTUAL STIMULATION Behavior a leader engages in to make followers aware of problems and view these problems in new ways, consistent with the leader's vision.

INTEREST GROUP An informal group composed of employees seeking to achieve a common goal related to their membership in an organization.

INTERNAL LOCUS OF CONTROL The tendency to locate responsibility for one's fate within oneself.

INTERNET A global system of computer networks.

INTRANET A companywide system of computer networks.

INTRAPRENEURS Employees of existing organizations who notice opportunities for product or service improvements and are responsible for managing the development process.

INTRINSICALLY MOTIVATED BEHAVIOR Behavior that is performed for its own sake.

INTUITION Ability to make sound decisions based on one's past experience and immediate feelings about the information at hand.

INVENTORY The stock of raw materials, inputs, and component parts that an organization has on hand at a particular time.

J

JARGON Specialized language that members of an occupation, group,

or organization develop to facilitate communication among themselves.

JOB ANALYSIS Identifying the tasks, duties, and responsibilities that make up a job and the knowledge, skills, and abilities needed to perform the job.

JOB DESIGN The process by which managers decide how to divide tasks into specific jobs.

JOB ENLARGEMENT Increasing the number of different tasks in a given job by changing the division of labor.

JOB ENRICHMENT Increasing the degree of responsibility a worker has over his or her job.

JOB SATISFACTION The collection of feelings and beliefs that managers have about their current jobs.

JOB SIMPLIFICATION The process of reducing the number of tasks that each worker performs.

JOB SPECIALIZATION The process by which a division of labor occurs as different workers specialize in different tasks over time.

JOINT VENTURE A strategic alliance among two or more companies that agree to jointly establish and share the ownership of a new business.

JUST-IN-TIME INVENTORY SYSTEM A system in which parts or supplies arrive at an organization when they are needed, not before.

JUSTICE RULE An ethical decision is a decision that distributes benefits and harms among people and groups in a fair, equitable, or impartial way.

K

KNOWLEDGE MANAGEMENT The sharing and integrating of expertise within and between functions and divisions through real-time, interconnected IT.

KNOWLEDGE MANAGEMENT SYSTEM A company-specific virtual information system that allows workers to share

their knowledge and expertise and find others to help solve ongoing problems.

L

LABOR RELATIONS The activities that managers engage in to ensure that they have effective working relationships with the labor unions that represent their employees' interests.

LATERAL MOVE A job change that entails no major changes in responsibility or authority levels.

LEADER An individual who is able to exert influence over other people to help achieve group or organizational goals.

LEADER-MEMBER RELATIONS The extent to which followers like, trust, and are loyal to their leader; a determinant of how favorable a situation is for leading.

LEADERSHIP The process by which an individual exerts influence over other people and inspires, motivates, and directs their activities to help achieve group or organizational goals.

LEADERSHIP SUBSTITUTE Characteristics of subordinates or characteristics of a situation or context that act in place of the influence of a leader and make leadership unnecessary.

LEADING Articulating a clear vision and energizing and enabling organizational members so that they understand the part they play in achieving organizational goals; one of the four principal functions of management.

LEARNING A relatively permanent change in knowledge or behavior that results from practice or experience.

LEARNING ORGANIZATION An organization in which managers try to maximize the ability of individuals and groups to think and behave creatively and thus maximize the potential for organizational learning to take place.

LEARNING THEORIES Theories that focus on increasing employee motivation and performance by linking

the outcomes that employees receive to the performance of desired behaviors and the attainment of goals.

LEGITIMATE POWER The authority that a manager has by virtue of his or her position in an organization's hierarchy.

LICENSING Allowing a foreign organization to take charge of manufacturing and distributing a product in its country or world region in return for a negotiated fee.

LINE MANAGER A person in the chain of command who has formal authority over people and resources.

LINGUISTIC STYLE A person's characteristic way of speaking.

LONG-TERM ORIENTATION A worldview that values thrift and persistence in achieving goals.

LOW-COST STRATEGY Driving the organization's costs down below the costs of its rivals.

M

MANAGEMENT The planning, organizing, leading, and controlling of human and other resources to achieve organizational goals effectively and efficiently.

MANAGEMENT BY OBJECTIVES A goal-setting process in which a manager and his or her subordinates negotiate specific goals and objectives for the subordinate to achieve and then periodically evaluate the extent to which the subordinate is achieving those goals.

MANAGEMENT BY WANDERING AROUND A face-to-face communication technique in which a manager walks around a work area and talks informally with employees about issues and concerns.

MANAGEMENT INFORMATION SYSTEM An information system that managers plan and design to provide themselves with the specific information they need.

MANAGEMENT SCIENCE THEORY An approach to management that uses rigorous quantitative techniques to

help managers make maximum use of organizational resources.

MANAGERIAL ROLE The specific tasks that a person is expected to perform because of the position he or she holds in an organization.

MARKET STRUCTURE An organizational structure in which each kind of customer is served by a self-contained division; also called *customer structure*.

MASLOW'S HIERARCHY OF NEEDS An arrangement of five basic needs that, according to Maslow, motivate behavior. Maslow proposed that the lowest level of unmet needs is the prime motivator and that only one level of needs is motivational at a time.

MASS-PRODUCTION TECHNOLOGY Technology that is based on the use of automated machines that are programmed to perform the same operations over and over.

MATRIX STRUCTURE An organizational structure that simultaneously groups people and resources by function and by product.

MECHANISTIC STRUCTURE An organizational structure in which authority is centralized, tasks and rules are clearly specified, and employees are closely supervised.

MEDIUM The pathway through which an encoded message is transmitted to a receiver.

MENTORING A process by which an experienced member of an organization (the mentor) provides advice and guidance to a less experienced member (the protégé) and helps the less experienced member learn how to advance in the organization and in his or her career.

MERIT PAY PLAN A compensation plan that bases pay on performance.

MESSAGE The information that a sender wants to share.

MIDDLE MANAGER A manager who supervises first-line managers and is

responsible for finding the best way to use resources to achieve organizational goals.

MISSION STATEMENT A broad declaration of an organization's purpose that identifies the organization's products and customers and distinguishes the organization from its competitors.

MIXED ECONOMY An economic system in which some sectors of the economy are left to private ownership and free-market mechanisms and others are owned by the government and subject to government planning.

MOOD A feeling or state of mind.

MORAL RIGHTS RULE An ethical decision is one that best maintains and protects the fundamental or inalienable rights and privileges of the people affected by it.

MORES Norms that are considered to be central to the functioning of society and to social life.

MOTIVATION Psychological forces that determine the direction of a person's behavior in an organization, a person's level of effort, and a person's level of persistence.

MULTIDOMESTIC STRATEGY Customizing products and marketing strategies to specific national conditions.

N

NATIONAL CULTURE The set of values that a society considers important and the norms of behavior that are approved or sanctioned in that society.

NEED A requirement or necessity for survival and well-being.

NEED FOR ACHIEVEMENT The extent to which an individual has a strong desire to perform challenging tasks well and to meet personal standards for excellence.

NEED FOR AFFILIATION The extent to which an individual is concerned about establishing and maintaining good

interpersonal relations, being liked, and having other people get along with each other.

NEED FOR POWER The extent to which an individual desires to control or influence others.

NEEDS ASSESSMENT An assessment to determine which employees need training or development and what type of skills or knowledge they need to acquire.

NEED THEORIES Theories of motivation that focus on what needs people are trying to satisfy at work and what outcomes will satisfy those needs.

NEGATIVE AFFECTIVITY The tendency to experience negative emotions and moods, to feel distressed, and to be critical of oneself and others.

NEGATIVE REINFORCEMENT Eliminating or removing undesired outcomes when people perform organizationally functional behaviors.

NEGOTIATION A method of conflict resolution in which the two parties in conflict consider various alternative ways to allocate resources to each other in order to come up with a solution acceptable to them both.

NETWORKING The exchange of information through a group or network of interlinked computers.

NETWORK STRUCTURE A series of strategic alliances that an organization creates with suppliers, manufacturers, and distributors to produce and market a product.

NEW VENTURE DIVISION An autonomous division that is given all the resources it needs to develop and market a new product.

NOISE Anything that hampers any stage of the communication process.

NOMINAL GROUP TECHNIQUE A decision-making technique in which group members write down ideas and solutions, read their suggestions to the whole group, and discuss and then rank the alternatives.

NONPROGRAMMED DECISION MAKING

Nonroutine decision making that occurs in response to unusual, unpredictable opportunities and threats.

NONVERBAL COMMUNICATION The encoding of messages by means of facial expressions, body language, and styles of dress.

NORMS Unwritten, informal codes of conduct that prescribe how people should act in particular situations.

NURTURING ORIENTATION A worldview that values the quality of life, warm personal friendships, and services and care for the weak.

O

OBJECTIVE APPRAISAL An appraisal that is based on facts and is likely to be numerical.

ON-THE-JOB TRAINING Training that takes place in the work setting as employees perform their job tasks.

OPENNESS TO EXPERIENCE The tendency to be original, to have broad interests, to be open to a wide range of stimuli, to be daring, and to take risks.

OPEN SYSTEM A system that takes in resources from its external environment and converts them into goods and services that are then sent back to that environment for purchase by customers.

OPERANT CONDITIONING THEORY

The theory that people learn to perform behaviors that lead to desired consequences and learn not to perform behaviors that lead to undesired consequences.

OPERATING BUDGET A budget that states how managers intend to use organizational resources to achieve organizational goals.

OPERATING SYSTEM SOFTWARE

Software that tells computer hardware how to run.

OPERATIONS INFORMATION SYSTEM A management information system that gathers, organizes, and summarizes

comprehensive data in a form that managers can use in their nonroutine coordinating, controlling, and decision-making tasks.

OPERATIONS MANAGEMENT The management of any aspect of the production system that transforms inputs into finished goods and services.

OPERATIONS MANAGER A manager who is responsible for managing an organization's production system and for determining where operating improvements might be made.

OPTIMUM DECISION The most appropriate decision in light of what managers believe to be the most desirable future consequences for their organization.

ORDER The methodical arrangement of positions to provide the organization with the greatest benefit and to provide employees with career opportunities.

ORGANIC STRUCTURE An organizational structure in which authority is decentralized to middle and first-line managers and tasks and roles are left ambiguous to encourage employees to cooperate and respond quickly to the unexpected.

ORGANIZATION CHANGE The movement of an organization away from its present state and toward some desired future state to increase its efficiency and effectiveness.

ORGANIZATIONAL ARCHITECTURE The organizational structure, control systems, and culture that together determine how efficiently and effectively organizational resources are used.

ORGANIZATIONAL BEHAVIOR The study of the factors that have an impact on how individuals and groups respond to and act in organizations.

ORGANIZATIONAL CITIZENSHIP BEHAVIORS Behaviors that are not required of organizational members but that contribute to and are necessary for organizational efficiency, effectiveness, and gaining a competitive advantage.

ORGANIZATIONAL COMMITMENT The collection of feelings and beliefs that managers have about their organizations as a whole.

ORGANIZATIONAL CONFLICT The discord that arises when the goals, interests, or values of different individuals or groups are incompatible and those individuals or groups block or thwart each other's attempts to achieve their objectives.

ORGANIZATIONAL CULTURE The set of values, norms, standards for behavior, and shared expectations that influence the ways in which individuals, groups, and teams interact with each other and cooperate to achieve organizational goals.

ORGANIZATIONAL DESIGN The process by which managers make specific organizing choices that result in a particular kind of organizational structure.

ORGANIZATIONAL ENVIRONMENT A set of forces and conditions that operate beyond an organization's boundaries but affect a manager's ability to acquire and utilize resources.

ORGANIZATIONAL LEARNING The process through which managers seek to improve employees' desire and ability to understand and manage the organization and its task environment.

ORGANIZATIONAL PERFORMANCE A measure of how efficiently and effectively a manager uses resources to satisfy customers and achieve organizational goals.

ORGANIZATIONAL POLITICS Activities that managers engage in to increase their power and to use power effectively to achieve their goals and overcome resistance or opposition.

ORGANIZATIONAL SOCIALIZATION The process by which newcomers learn an organization's values and norms and acquire the work behaviors necessary to perform jobs effectively.

ORGANIZATIONAL STAKEHOLDERS Shareholders, employees, customers, suppliers, and others who have an

interest, claim, or stake in an organization and in what it does.

ORGANIZATIONAL STRUCTURE A formal system of task and reporting relationships that coordinates and motivates organizational members so that they work together to achieve organizational goals.

ORGANIZING Structuring working relationships in a way that allows organizational members to work together to achieve organizational goals; one of the four principal functions of management.

OUTCOME Anything a person gets from a job or organization.

OUTSOURCE To use outside suppliers and manufacturers to produce goods and services.

OVERPAYMENT INEQUITY The inequity that exists when a person perceives that his or her own outcome/input ratio is greater than the ratio of a referent.

OVERT DISCRIMINATION Knowingly and willingly denying diverse individuals access to opportunities and outcomes in an organization.

P

PATH-GOAL THEORY A contingency model of leadership proposing that leaders can motivate subordinates by identifying their desired outcomes, rewarding them for high performance and the attainment of work goals with these desired outcomes, and clarifying for them the paths leading to the attainment of work goals.

PAY LEVEL The relative position of an organization's pay incentives in comparison with those of other organizations in the same industry employing similar kinds of workers.

PAY STRUCTURE The arrangement of jobs into categories reflecting their relative importance to the organization and its goals, level of skill required, and other characteristics.

PERCEPTION The process through which people select, organize, and

interpret what they see, hear, touch, smell, and taste, to give meaning and order to the world around them.

PERFORMANCE APPRAISAL The evaluation of employees' job performance and contributions to their organization.

PERFORMANCE FEEDBACK The process through which managers share performance appraisal information with subordinates, give subordinates an opportunity to reflect on their own performance, and develop, with subordinates, plans for the future.

PERSONALITY TRAITS Enduring tendencies to feel, think, and act in certain ways.

PLANNING Identifying and selecting appropriate goals and courses of action; one of the four principal functions of management.

POLITICAL AND LEGAL FORCES Outcomes of changes in laws and regulations, such as the deregulation of industries, the privatization of organizations, and increased emphasis on environmental protection.

POLITICAL STRATEGIES Tactics that managers use to increase their power and to use power effectively to influence and gain the support of other people while overcoming resistance or opposition.

POSITION POWER The amount of legitimate, reward, and coercive power that a leader has by virtue of his or her position in an organization; a determinant of how favorable a situation is for leading.

POSITIVE REINFORCEMENT Giving people outcomes they desire when they perform organizationally functional behaviors.

POTENTIAL COMPETITORS Organizations that presently are not in a task environment but could enter if they so chose.

POWER DISTANCE The degree to which societies accept the idea that inequalities in the power and well-being of their citizens are due to differences in individuals' physical and intellectual capabilities and heritage.

PRACTICAL RULE An ethical decision is one that a manager has no reluctance about communicating to people outside the company because the typical person in a society would think it is acceptable.

PROCEDURAL JUSTICE A moral principle calling for the use of fair procedures to determine how to distribute outcomes to organizational members.

PROCESS REENGINEERING The fundamental rethinking and radical redesign of business processes to achieve dramatic improvements in critical measures of performance such as cost, quality, service, and speed.

PRODUCT CHAMPION A manager who takes "ownership" of a project and provides the leadership and vision that take a product from the idea stage to the final customer.

PRODUCT DEVELOPMENT PLAN A plan that specifies all of the relevant information that managers need in order to decide whether to proceed with a full-blown product development effort.

PRODUCTION BLOCKING A loss of productivity in brainstorming sessions due to the unstructured nature of brainstorming.

PRODUCTION SYSTEM The system that an organization uses to acquire inputs, convert the inputs into outputs, and dispose of the outputs.

PRODUCT LIFE CYCLE Changes in demand for a product that occur from its introduction through its growth and maturity to its decline.

PRODUCT STRUCTURE An organizational structure in which each product line or business is handled by a self-contained division.

PRODUCT TEAM STRUCTURE An organizational structure in which employees are permanently assigned to a cross-functional team and report only to the product team manager or to one of his or her direct subordinates.

PROFESSIONAL ETHICS Standards that govern how members of a profession are

to make decisions when the way they should behave is not clear-cut.

PROGRAMMED DECISION MAKING Routine, nearly automatic decision making that follows established rules or guidelines.

PUNISHMENT Administering an undesired or negative consequence when dysfunctional behavior occurs.



QUANTUM PRODUCT INNOVATIONS Products that result from quantum technological changes.

QUANTUM TECHNOLOGICAL CHANGE A fundamental shift in technology that results in the innovation of new kinds of goods and services.

QUID PRO QUO SEXUAL HARASSMENT Asking for or forcing an employee to perform sexual favors in exchange for some reward or to avoid negative consequences.



REAL-TIME INFORMATION Frequently updated information that reflects current conditions.

REASONED JUDGMENT A decision that takes time and effort to make and results from careful information gathering, generation of alternatives, and evaluation of alternatives.

RECEIVER The person or group for which a message is intended.

RECRUITMENT Activities that managers engage in to develop a pool of qualified candidates for open positions.

REFERENT POWER Power that comes from subordinates' and co-workers' respect, admiration, and loyalty.

RELATED DIVERSIFICATION Entering a new business or industry to create a competitive advantage in one or more of an organization's existing divisions or businesses.

RELATIONSHIP-ORIENTED LEADERS

Leaders whose primary concern is to develop good relationships with their subordinates and to be liked by them.

RELIABILITY The degree to which a tool or test measures the same thing each time it is used.

REPRESENTATIVE DEMOCRACY A political system in which representatives elected by citizens and legally accountable to the electorate form a government whose function is to make decisions on behalf of the electorate.

REPUTATION The esteem or high repute that individuals or organizations gain when they behave ethically.

RESEARCH AND DEVELOPMENT TEAM

A team whose members have the expertise and experience needed to develop new products.

RESTRUCTURING Downsizing an organization by eliminating the jobs of large numbers of top, middle, and first-line managers and nonmanagerial employees.

REWARD POWER The ability of a manager to give or withhold tangible and intangible rewards.

RISK The degree of probability that the possible outcomes of a particular course of action will occur.

ROLE The specific tasks that a person is expected to perform because of the position he or she holds in an organization.

ROLE MAKING Taking the initiative to modify an assigned role by assuming additional responsibilities.

RULES Formal written instructions that specify actions to be taken under different circumstances to achieve specific goals.

RUMORS Unofficial pieces of information of interest to organizational members but with no identifiable source.

S

SATISFICING Searching for and choosing an acceptable, or satisfactory,

response to problems and opportunities, rather than trying to make the best decision.

SCENARIO PLANNING The generation of multiple forecasts of future conditions followed by an analysis of how to respond effectively to each of those conditions; also called *contingency planning*.

SCHEMA An abstract knowledge structure that is stored in memory and makes possible the interpretation and organization of information about a person, event, or situation.

SCIENTIFIC MANAGEMENT The systematic study of relationships between people and tasks for the purpose of redesigning the work process to increase efficiency.

SELECTION The process that managers use to determine the relative qualifications of job applicants and their potential for performing well in a particular job.

SELF-EFFICACY A person's belief about his or her ability to perform a behavior successfully.

SELF-ESTEEM The degree to which individuals feel good about themselves and their capabilities.

SELF-MANAGED WORK TEAM A group of employees who supervise their own activities and monitor the quality of the goods and services they provide.

SELF-REINFORCER Any desired or attractive outcome or reward that a person gives to himself or herself for good performance.

SENDER The person or group wishing to share information.

SHORT-TERM ORIENTATION A worldview that values personal stability or happiness and living for the present.

SKUNKWORKS A group of intrapreneurs who are deliberately separated from the normal operation of an organization to encourage them to devote all their attention to developing new products.

SMALL-BATCH TECHNOLOGY Technology that is used to produce small quantities of customized, one-of-a-kind products and is based on the skills of people who work together in small groups.

SOCIAL LEARNING THEORY A theory that takes into account how learning and motivation are influenced by people's thoughts and beliefs and their observations of other people's behavior.

SOCIAL LOAFING The tendency of individuals to put forth less effort when they work in groups than when they work alone.

SOCIAL RESPONSIBILITY A manager's duty or obligation to make decisions that promote the welfare and well-being of stakeholders and society as a whole.

SOCIAL STRUCTURE The arrangement of relationships between individuals and groups in a society.

SOCIETAL ETHICS Standards that govern how members of a society are to deal with each other on issues such as fairness, justice, poverty, and the rights of the individual.

SOCIOCULTURAL FORCES Pressures emanating from the social structure of a country or society or from the national culture.

SPAN OF CONTROL The number of subordinates who report directly to a manager.

STAFF MANAGER A person not in the chain of command who provides line managers with expertise and support in areas such as finances, planning, and marketing.

STAGE-GATE DEVELOPMENT FUNNEL A planning model that forces managers to make choices among competing projects so that organizational resources are not spread thinly over too many projects.

STANDARD OPERATING PROCEDURES Specific sets of written instructions about how to perform a certain aspect of a task.

STEREOTYPE Simplistic and often inaccurate beliefs about the typical characteristics of particular groups of people.

STRATEGIC ALLIANCE An agreement in which managers pool or share their organization's resources and know-how with a foreign company, and the two organizations share the rewards and risks of starting a new venture.

STRATEGIC HUMAN RESOURCE MANAGEMENT The process by which managers design the components of a human resource management system to be consistent with each other, with other elements of organizational architecture, and with the organization's strategy and goals.

STRATEGY A cluster of decisions about what goals to pursue, what actions to take, and how to use resources to achieve goals.

STRATEGY FORMULATION Analysis of an organization's current situation followed by the development of strategies to accomplish its mission and achieve its goals.

SUBJECTIVE APPRAISAL An appraisal that is based on perceptions of traits, behaviors, or results.

SUPPLIERS Individuals and organizations that provide an organization with the input resources that it needs to produce goods and services.

SWOT ANALYSIS A planning exercise in which managers identify organizational strengths (S), weaknesses (W), environmental opportunities (O), and threats (T).

SYNERGY Performance gains that result when individuals and departments coordinate their actions.

T

TARIFF A tax that a government imposes on imported or, occasionally, exported goods.

TASK ENVIRONMENT The set of forces and conditions that originate with

suppliers, distributors, customers, and competitors and affect an organization's ability to obtain inputs and dispose of its outputs because they influence managers on a daily basis.

TASK FORCE A committee of managers or nonmanagerial employees from various departments or divisions who meet to solve a specific, mutual problem; also called an *ad hoc committee*.

TASK-ORIENTED LEADERS Leaders whose primary concern is to ensure that subordinates perform at a high level.

TASK STRUCTURE The extent to which the work to be performed is clear-cut so that a leader's subordinates know what needs to be accomplished and how to go about doing it; a determinant of how favorable a situation is for leading.

TEAM A group whose members work intensely with each other to achieve a specific, common goal or objective.

TECHNICAL SKILLS Job-specific knowledge and techniques that are required to perform an organizational role.

TECHNOLOGICAL FORCES Outcomes of changes in the technology that managers use to design, produce, or distribute goods and services.

TECHNOLOGY The combination of skills and equipment that managers use in the design, production, and distribution of goods and services.

TERMINAL VALUE A lifelong goal or objective that an individual seeks to achieve.

THEORY X Negative assumptions about workers that lead to the conclusion that a manager's task is to supervise them closely and control their behavior.

THEORY Y Positive assumptions about workers that lead to the conclusion that a manager's task is to create a work setting that encourages commitment to organizational goals and provides opportunities for workers to be imaginative and to exercise initiative and self-direction.

360-DEGREE APPRAISAL A performance appraisal by peers, subordinates, superiors, and sometimes clients who are in a position to evaluate a manager's performance.

TIME HORIZON The intended duration of a plan.

TOP-DOWN CHANGE Change that is implemented quickly throughout an organization by upper-level managers.

TOP-MANAGEMENT TEAM A group composed of the CEO, the president, and the heads of the most important departments.

TOP MANAGER A manager who establishes organizational goals, decides how departments should interact, and monitors the performance of middle managers.

TOTALITARIAN REGIME A political system in which a single party, individual, or group holds all political power and neither recognizes nor permits opposition.

TRAINING Teaching organizational members how to perform their current jobs and helping them acquire the knowledge and skills they need to be effective performers.

TRANSACTIONAL LEADERSHIP Leadership that motivates subordinates by rewarding them for high performance and reprimanding them for low performance.

TRANSACTION-PROCESSING SYSTEM A management information system designed to handle large volumes of routine, recurring transactions.

TRANSFORMATIONAL LEADERSHIP Leadership that makes subordinates aware of the importance of their jobs and performance to the organization and aware of their own needs for personal growth and that motivates subordinates to work for the good of the organization.

TRANSITORY CAREER A career in which a person changes jobs frequently and in which each job is different from the one that precedes it.

TRUST A person's confidence and faith in another person's good will.

U

UNCERTAINTY Unpredictability.

UNCERTAINTY AVOIDANCE The degree to which societies are willing to tolerate uncertainty and risk.

UNDERPAYMENT INEQUITY The inequity that exists when a person perceives that his or her own outcome/input ratio is less than the ratio of a referent.

UNETHICAL DECISION A decision that a manager would prefer to disguise or hide from other people because it enables a company or a particular individual to gain at the expense of society or other stakeholders.

UNITY OF COMMAND A reporting relationship in which an employee receives orders from, and reports to, only one superior.

UNITY OF DIRECTION The singleness of purpose that makes possible the creation

of one plan of action to guide managers and workers as they use organizational resources.

UNRELATED DIVERSIFICATION Entering a new industry or buying a company in a new industry that is not related in any way to an organization's current businesses or industries.

UTILITARIAN RULE An ethical decision is a decision that produces the greatest good for the greatest number of people.

V

VALENCE In expectancy theory, how desirable each of the outcomes available from a job or organization is to a person.

VALIDITY The degree to which a tool or test measures what it purports to measure.

VALUES Ideas about what a society believes to be good, right, desirable, or beautiful.

VALUE SYSTEM The terminal and instrumental values that are guiding principles in an individual's life.

VERBAL COMMUNICATION The encoding of messages into words, either written or spoken.

VERTICAL INTEGRATION A strategy that allows an organization to create value by producing its own inputs or distributing and selling its own outputs.

VICARIOUS LEARNING Learning that occurs when the learner becomes motivated to perform a behavior by watching another person perform it; also called *observational learning*.

VIRTUAL TEAM A team whose members rarely or never meet face-to-face and interact by using various forms of information technology such as email, computer networks, telephone, fax, and videoconferences.

W

WHOLLY OWNED FOREIGN SUBSIDIARY Production operations established in a foreign country independent of any local direct involvement.

Credits

Notes

Chapter 1

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Index

Names

A

Aaron, K., 555
Abell, D. F., 559, 571
Abott, Ida, 435
Ackerman, P. L., 563
Adams, D. A., 570
Adams, J. Stacy, 332, 562
Adams, S., 564
Adler, Nancy J., 562
Adler, P. S., 552
Agarwala-Rogers, R., 570
Aguilar, F. J., 559
Ahlers, Linda L., 263
Alahuhta, Matti, 306
Albertson, Joe, 383, 384
Alexander, J. A., 561
Alfadian, Pascal, 453
Allen, Robert, 442, 569
Allen, T. D., 569
Alvarez, Ralph, 264, 265
Ammenheuser, M. K., 563
Amoruso, Cheryl, 115
Ancona, D. G., 548
Anderson, Brad, 326
Anderson, C., 549
Anderson, Michael, 184
Anderson, P., 568
Anderson, Richard Dean, 485
Andrews, K. R., 553, 559
Anthony, R. N., 561
Aoki, M., 572
Aplin, J. C., 558
Argyris, C., 569
Armour, S., 554
Armstrong, L., 566
Arndt, Michael, 37, 39, 168, 558, 565, 566, 568
Arner, Faith, 280, 281
Arnold, Ulli, 382
Arnst, C., 556, 560
Arrow, Kenneth J., 557
Arthur, M. B., 572
Artzt, Edwin, 52
Ash, R., 572
Aston, Adam, 281
Atlas, R. D., 550
Austin, N., 571
Avolio, B. J., 566
Ayman, R., 566

B

Baetz, M. L., 565
Bahree, B., 559
Baig, E., 571
Bain, J. E., 556
Baird, L., 568
Baker, S., 563, 568
Ballmer, Steve, 360

Balsillie, Jim, 198–199
Bandura, A., 563
Banerjee, N., 569
Bangle, Chris, 369, 565
Barbeite, F. G., 562
Barley, S. R., 553
Barnard, C. I., 552
Barnes-Farrell, J., 554
Baron, R. A., 551
Barr, M., 557
Barrett, Colleen C., 267, 387, 566
Barrick, M. R., 550
Barry, V., 549, 552
Barsaloux, J., 558
Bartlett, C. A., 556, 559
Bass, B. J., 566
Bass, B. M., 565, 566
Baucus, M. S., 553
Baum, H. G., 549
Bazerman, Max H., 557, 558
Bean, Leo Leonwood, 201
Beauchamp, T. L., 552
Bechler, Steven, 30
Becker, T. E., 553
Begley, S., 551
Bell, C. H., 561
Bellah, R., 556
Belson, K., 563, 564
Bendixen, Sergio, 134
Benjamin, R. I., 570
Bennett, Russell A., 134
Bennis, W., 564
Bercovici, J., 551
Berger, B., 558
Berger, P. L., 552
Berkowitz, L., 565
Berman, D. K., 555
Bernier, Robert, 168, 568
Bernstein, Aaron, 573
Berry, L., 549
Berton, L., 551
Bettenhausen, K., 551
Betts, M., 563
Beyer, J. M., 551, 552
Bezos, Jeff, 56, 144, 392–393
Bhagwati, Jagdish, 556
Bharat, Krishna, 453
Bianco, Anthony, 85, 168
Biondi, Frank, 239
Bird, L., 565
Birdsall, David B., 84
Black, K., 567
Blackburn, R. S., 567
Blake, R. R., 565
Blake, S., 549
Blanchard, K., 565
Blank, Arthur, 3
Blau, P. M., 560, 561
Bloom, J., 562
Blumenstein, R., 570
Blunt, J., 570
Bodecker, Sandy, 328–329
Bohr, Bernd, 510
Bolton, Lesley, 573
Bonaminio, Jim, 83–85
Bonisson, P. P., 571
Boone, Garrett, 349–350
Borman, C., 569
Borman, W. C., 569
Boslet, M., 563
Bouchard, T. J., Jr., 558
Bourgeois, L. J., 555
Bowden, A., 556
Bower, Amanda, 572
Bowie, N. E., 552
Boyle, Dennis, 76
Boyle, M., 558
Bracken, D. W., 569
Bradspies, R. W., 561
Brady, D., 87, 131, 199, 383, 568
Brandt, R., 563, 570
Bremner, B., 169, 565
Bresler, S. J., 555
Brett, J. B., 64
Brickner, M. A., 568
Brief, A. P., 68, 550, 551
Brockner, J., 550
Bromley, Stan, 435
Brooker, Katrina, 573
Brown, Andy, 198
Brown, David, 184
Brown, L., 561
Brown, Richard H., 443
Brown, V., 555
Brownstein, R., 554
Bruer, J. T., 555
Brumit Kropf, M., 553
Brun, S. E., 568
Buday, R. S., 566
Bulkeley, W. M., 560, 561
Bunderson, S. J., 549
Burcke, J. M., 566
Burke, M. J., 68
Burke, Monte, 573
Burlingham, B., 551
Burnett, D. D., 550
Burnham, D. H., 550, 562
Burns, L. R., 560
Burns, T., 560
Burns, Ursula M., 281
Burton, T. M., 565
Butler, J. E., 568
Butzer, Bait, 263
Buzzotta, V. R., 567
Byrne, J. A., 548, 570

C

Calori, R., 564
Camarena, Jose, 121–123
Campbell, J. P., 548, 562

Campbell, Tracey, 122
Canion, Rod, 313
Capowski, G. S., 561
Card, David, 487
Cardy, R. L., 554
Carey, A., 549
Carpenter, M. A., 556
Carpenter, S., 550
Carroll, J. S., 548, 561
Carroll, S. J., 548
Carruthers, Sally, 361
Carter, B., 560
Carton, B., 554, 555
Cartwright, D., 564, 567
Casey, James E., 304
Castell, William M. "Bill," 85, 87, 382
Cavanaugh, G. F., 552
Caves, R. E., 559
Chambers, John, 211
Champy, J., 566, 572
Chan, C., 559
Chandler, Alfred D., 476, 559, 560, 571
Chavez, L., 554
Chawla, Kalpana, 184
Chemers, M. M., 566
Chen, A., 556
Chenault, Kenneth I., 22
Chesonis, Arunas, 51–52, 56, 58, 59
Child, J., 552, 560, 570
Cho, Jujio, 489
Chon, Choon T., 510
Chong, Keith, 358
Chopra, Deepak, 199
Christensen, C. R., 559
Cisneros, Henry, 132
Claburn, T., 566, 567
Claiborne, Liz, 173, 311
Clare, David, 108
Clark, K. D., 549
Clark, Laurel, 184
Clark, P. A., 561
Clay, R. A., 562
Clegg, C. W., 567
Cleveland, J. N., 554
Clifford, L., 568
Cohen, J. D., 551
Cohen, M. D., 557
Cohen, R. L., 563
Cohn, L. Q., 556
Cole, J. R., 555
Colella, A., 554
Colihan, J., 567
Collins, C. J., 549
Collins, D., 553
Colquhite, J. A., 550
Combs, J. G., 548
Compton, Mark, 367
Comstock, Beth, 86

Conant, Douglas, 213–216
 Conger, J. A., 566
 Conlin, M., 486, 553
 Connolly, T., 563
 Cook, J. D., 66
 Cooper, C. L., 569, 572
 Cooper, J. C., 566, 568
 Copeland, M., 562
 Coplan, J. H., 554
 Coradetti, W. R., 566
 Corbo, Patrick, 67
 Corddry, Paul I., 383
 Corliss, Richard, 573
 Cosier, R. A., 558
 Costa, P. T., 550
 Cotsonas, David, 369–370
 Coutts, P., 564
 Cox, T. H., 549
 Coy, P., 566
 Crockett, R. O., 560
 Crosby, Philip B., 498, 571
 Crotty, W. D., 559
 Cullen, J. B., 553
 Cummings, L. L., 551, 553, 565, 571
 Cuneo, A. Z., 555
 Cyert, R., 557, 570

D

Dadiseth, Keki, 220
 Daft, Douglas, 443
 Daft, R. L., 557, 571
 Dalesio, E. P., 561
 Dalkey, N., 558
 Dallas, S., 566
 D'Amico, Mario, 573
 Darley, J. M., 551
 Daruwala, Nikki, 122–123
 Daus, C. S., 549
 Davidow, W. H., 570
 Davis, S. M., 560
 Davis, T. R. V., 563
 Dawley, H., 558
 Dawson, C., 510, 565
 Day, Frank B., 393
 de Bendem, P., 561
 de Bono, Edward, 182, 558
 De Cordoba, J., 572
 De Geus, A. P., 559
 de Janasz, S. C., 549, 572
 De Marco, D., 564
 Dechant, K., 555
 Del Valle, C., 569
 Delbecq, A., 558
 Dell, Michael, 8–9, 9*f*, 12–13, 14, 15–16, 23, 24, 26, 146
 DeMarie, S. M., 567
 Der Hovanesian, Mara, 135
 Deutschman, A., 566, 567
 Deveny, T., 556
 Dharan, Bala, 563
 Diaz, Al, 182
 Diehl, M., 558
 Digman, J. M., 550
 Dobson, J., 553
 Donahue, Randy, 116
 Donaldson, T., 549, 552
 Done, K., 571
 Donnelly, Sally B., 573
 Donovan, J. J., 563, 571
 Dornbusch, S. M., 570

Dorsey, D., 550
 Dougherty, T. W., 572
 Doz, Y. L., 559
 Draper, Heather, 572
 Drauden, G., 558
 Dreher, G., 572
 Driver, M. J., 572
 Drucker, Peter F., 548, 561
 Druskat, V. U., 548
 Duarte, D. L., 567
 Duff, M., 564, 572
 Dufour, B., 564
 Dumaine, B., 548, 561, 567, 570, 572
 Duncan, R., 560
 Dunham, Randall B., 64
 Dunn, M., 558
 Dunnette, Marvin D., 548, 562, 563, 565, 567, 569

E

Eagly, A. H., 566
 Earley, P. C., 551, 563, 567
 Ebbers, Bernie, 93, 96
 Eby, L. T., 569, 572
 Echikson, W., 561, 572
 Eckert, Bob, 210–211
 Edid, M., 572
 Edmondson, Gail, 238, 556
 Edwards, C., 417, 555
 Edwards, D., 562
 Edwards, M. R., 569
 Eidam, Michael, 135, 452
 Einstein, W. O., 566
 Eisner, Michael, 96, 318
 Ekegren, G., 563
 Eleta, Graciela, 134
 Elgin, B., 561, 570
 Elgon, Ben, 487
 Elkind, P., 552
 Ellison, Larry, 283–284, 298, 311, 313
 Elmore, Barbara, 573
 Emrich, C., 555
 Emshwiller, J. R., 552, 573
 Engardio, P., 563
 Epstein, S., 551
 Erez, M., 559
 Erlich, Andrew, 133
 Ernschaw, A., 557
 Evans, M. G., 565
 Ewing, Jack, 40, 383

F

Fairhurst, G. T., 561
 Farnham, A., 560
 Fassheber, Peter, 40
 Fastow, Andrew, 93
 Fayol, Henri, 19, 203, 208, 548, 559
 Feather, N. T., 562
 Feldman, D. C., 552
 Fenn, D., 566
 Ference, T. P., 572
 Fernandez, J. P., 557
 Ferris, G. R., 550, 568
 Festinger, L., 567
 Fiedler, Fred E., 365–367, 565
 Fierman, J., 565

Fife, William J., 360
 Files, J., 554
 Finestone, William, 67
 Finholt, T., 567
 Finkelstein, S., 568
 Fiorina, Carly S., 56, 111, 443
 Fish, Lawrence, 365
 Fisher, C. D., 563, 568, 569
 Fiske, S. T., 555
 Fitzgerald, Peter, 62
 Duff, M., 564, 572
 Flammholtz, E., 561
 Flannigan, C., 566
 Fleming, Marcella, 352
 Flint, J., 554, 569
 Florian, E., 549
 Floyd, S. W., 561
 Flynn, J., 570
 Follett, Mary Parker, 45, 46, 549
 Ford, Bill, 376
 Ford, Henry, 48
 Ford, Sara, 485
 Forgas, J. P., 551
 Foroohar, Rana, 573
 Fossum, Eric, 395
 Foust, Dean, 319, 452
 Fox, M. E., 555
 France, M., 353
 Frankel, M. S., 553, 555
 Fraser, Jill Andresky, 335
 Fredrickson, J. W., 556
 Freeman, R. E., 552
 French, R. P., Jr., 564
 French, W. L., 561
 Frith, Jacob, 9*f*
 Fry, L., 549, 571
 Fung, Victor, 142–143
 Fung, William, 142–143
 Furst, S. A., 567
 Futter, Ellen V., 130

G

Gabor, A., 571
 Gagne, Vincent, 573
 Galbraith, J. R., 560
 Galen, M., 555
 Ganster, D. C., 552
 Garcia, Sandi, 63
 Garfinkel, P., 569
 Garnier, Jean-Pierre, 197–198
 Garvin, D., 571
 Gates, William H., III “Bill,” 21, 56, 74, 94, 173, 283, 284, 311, 360, 422, 485–486
 Gavin, M. B., 561
 Geare, A. J., 563
 Geber, B., 567
 Gebhardt, Henning, 382
 Geffen, David, 117–118
 Gehry, Frank, 190
 Geier, Jon A., 352
 Geis, F. L., 555
 Gellerman, S. W., 553
 Gendron, M., 563
 Gentile, Mary C., 558
 George, J. M., 68, 548, 551, 554, 567, 568, 569
 Gerkovich, P. R., 553
 Gersick, C. J. G., 567
 Gerstner, Louis V., Jr., 57, 79, 429

Gertner, J., 564
 Ghemawat, P., 560
 Ghoshal, S., 556, 559, 561
 Giangola, Andrew, 470
 Gibson, C., 553
 Gier, J. A., 569
 Gilbert, R. J., 556
 Gillan, Brian, 84
 Gillmore, Dan, 486
 Gilmour, Allan, 117–118
 Gist, M. E., 563
 Glanz, J., 558
 Goldberg, Lewis R., 54
 Goldhirsh, Bernard “Bernie,” 69–70, 551
 Goldstein, A. P., 563
 Goldstein, H. B., 552
 Goldstein, I. L., 569
 Goldwasser, A., 563
 Goleman, D., 551
 Gomez-Mejia, Luis, 548
 Goodheim, L., 566
 Goodman, N., 556
 Goodman, P. S., 548, 568
 Goodnight, James, 322
 Goodwin, R. E., 552
 Gordon, M. B., 571
 Gourlay, R., 571
 Govindarajan, V., 555
 Graham, P., 549
 Graham-Moore, B. E., 563
 Green, J., 556
 Green, S. G., 561
 Greenberg, Jeffrey, 129, 563
 Greenberg, Maurice R. “Hank,” 129–131
 Greene, J. D., 551
 Greenfield, Richard, 487
 Greenhaus, J. H., 572
 Greenwood, N., 571
 Greer, B., 569
 Greer, C. R., 554
 Greising, D., 563, 572
 Grey, S., 560
 Griffin, N. Shope, 562
 Griffin, R. W., 555, 558, 560
 Griffiths, J., 571
 Grove, A., 564
 Grover, Ronald, 135, 168, 239
 Guest, R. H., 549
 Guion, R. M., 569
 Gull, N., 557
 Gunther, M., 563
 Gupta, A. K., 548, 555
 Gupta, Nitin, 453
 Gustafson, D. H., 558
 Gutner, T., 553
 Guzman, B., 553
 Guzman, Leopoldo E., 134

H

Hackman, J. R., 250–251, 560, 567
 Halamka, John, 186–187, 558
 Hales, C. P., 548
 Hall, R. H., 560
 Hambrick, D. C., 548
 Hamel, Gary, 559
 Hammer, M., 566, 572
 Hammer, W. C., 563
 Hamway, Jeanne, 109

- Hannah, J., 570
Hanson, Victor Davis, 133
Harden, Judy, 117
Harkins, S., 568
Harrington, A., 569
Harrington, Noreen, 58–59, 550
Hartke, D. D., 565
Harvey, R. J., 569
Hater, J. J., 566
Hauck, Chris, 307
Hauck, L. C., 561
Hauck, R. M., 561
Hawn, C., 548
Hax, A. C., 567
Hayes, R. H., 571
Haythornthwaite, Alice, 573
Hedberg, B., 558
Helgren, Michael D., 352–353
Heller, L., 562
Helm, L., 572
Hempel, J., 554
Hendrickson, A. R., 567
Henkoff, R., 567
Hepworth, S. J., 66
Hersey, P., 565
Herzberg, Frederick, 329, 331, 562
Heskett, J. L., 561
Hetzer, B., 555
Hewitt, P., 554
Hewlett, William “Bill,” 79–80, 313, 468
Heyer, Steven, 443
Hickman, J., 549
Hicks, M., 556
Hickson, D. J., 561
Highhouse, S., 552
Hightower, R., 567
Hill, C. W. L., 556, 559, 560, 561, 570, 571, 572
Hill, E. J., 567
Hill, L., 549
Hillson, Paul J., 452
Hines, G. H., 550, 562
Hinings, C. R., 561
Hinz, Werner, 390
Hoerr, J., 572
Hof, R. D., 317–318, 557, 563
Hofer, C. W., 559
Hofstede, Geert, 161–163, 556, 562
Holland, J. L., 572
Holloway, A., 562
Holmes, S., 353, 384
Holyoke, L., 566
Hood, N., 559
Hopkirk, Paddy, 498
Hoppe, M. H., 556
Hough, L. M., 562, 563, 565, 567, 569
Houlder, Y., 572
House, Robert J., 365, 367–368, 370, 550, 562, 564, 565
Hout, T. H., 570
Hout, T. M., 572
Hubbell, Rachel, 387
Hubbell, Steve, 387
Huber, G. P., 557
Hughes, Robert, 453
Hume, Susan, 573
Hundal, P. S., 550, 562
Hunter, J. E., 561, 570
Hunter, William, 190–191
Huntington, Samuel P., 133
Husband, Rick, 184
Hymowitz, C., 550, 558, 565
- I**
Ihlwan, Moon, 169, 555, 558
Immelt, Jeffrey, 85–87, 203, 206, 294
Inouye, Wayne, 244–245
Irvine, M., 551
Isen, A. M., 551
Ismail, Lobna, 114
Ittycheria, Dey, 427
Ivestor, Douglas, 443
- J**
Jackson, J., 568
Jackson, J. H., 569
Jackson, Jesse, 114
Jackson, P. R., 548, 567
Jackson, S. E., 549, 569
Jaffe, E., 557
Jamieson, D., 549
Janders, Jeffrey K., 32
Janis, I. L., 558
Jarrell, Buster, 396
Jaussi, A. S., 549
Jensen, Carol, 350–353
Jensen, M. C., 567
Jerdee, T. H., 548
Jermier, J. M., 565
Jobs, Steven P., 25–27, 29
Joel, A. C., 549
Johnson, B. T., 566
Johnson, H. E., 571
Johnson, Lyndon B., 187
Johnson, Robert Wood, 108
Johnston, Lawrence R., 383–384
Jones, D., 553, 560
Jones, Gareth R., 548, 552, 553, 559, 560, 561, 568, 570, 571
Jones, J. R., 552
Jones, Reg, 219
Jones, T. M., 553
Joshi, Vyomesh, 280
Jung, Andrea, 10, 11, 70, 111, 374, 551
- K**
Kahn, J., 555, 573
Kahneman, Daniel, 175–176, 557
Kaihla, P., 566, 567
Kanfer, R., 562, 563
Kanungo, R. N., 566
Kapsalis, S. C., 559
Karau, S. J., 566
Karl, K. A., 567
Katz, R. L., 549
Kaufman, J., 562
Kazanjan, R. K., 560
Kelleher, Herb, 52, 106, 388
Kelleher, K., 558–559
Kelleher, N., 548
Kelley, David, 72, 73, 552
Kelley, T., 552, 567
Kelly, E. P., 552
Kelly, Richard, 99
Kemp, N. J., 567
Kennedy, John F., 187
Kerkorian, Kirk, 239
Kerr, N. L., 568
Kerr, S., 565, 570
Kilts, James M., 297
Kim, W. Chan, 573
Kim Ssang Su, 138
King, Claudia, 332–333
King, N., 562
King, Robert, 402
King, S. N., 548
Kirkpatrick, D., 568
Kirkpatrick, S. A., 565
Kiuchi, Masao, 512
Kleiman, C., 570
Klein, Gary, 96
Kleinfeld, Klaus, 39–40, 381–383
Kline, Daniel, 118
Knight, Philip, 273–274
Knouf, Craig, 171–172, 173, 174
Ko, S. J., 553
Kogut, B., 559, 560
Konrads, W., 556
Koontz, H., 561
Koppes, L., 562
Koretz, G., 554
Korzenny, Felipe, 133
Kotter, J. P., 548, 561
Kraul, A. I., 548
Kraus, Michael, 357
Kravets, D., 552
Kreitner, R., 563
Kreps, G. L., 555
Kripalani, M., 569
Kroc, Ray, 74, 77
Krugman, Paul, 556
Kunii, I. M., 556
- L**
Laabs, J., 561
Labate, J., 563
Labich, K., 548
Lack, Andrew, 239
Laing, John R., 281
Lambert, A., 555
Lamm, Richard D., 133
Lane, D. M., 555
Langowitz, N. J., 557
Latane, B., 568
Latham, G. P., 335, 559, 562, 563, 569
Lavelle, L., 570
Law, K., 70
Lawler, Edward E., III, 417, 561, 563
Lawrence, P. R., 560
Laybourne, Geraldine, 366
Lazaridis, Mike, 198–199
Lazarus, Rochelle, 361
Le Maistre, Ray, 550
Lee Ku Taek, 168
LeFauve, R. G., 567
LeIchuk, I., 554
LeMothe, William E. 464
Lengel, R. H., 557, 571
Lentz, E., 569
Lever, William, 156–157
Levering, R., 564
Levin, L., 569
Levine, E. L., 566, 569
Levitt, T., 555
Lewent, Judy, 479–480
Lewis, Kenneth D., 451
Lieberfarb, Warren, 239
Ligocki, Kathleen, 375–376, 566
Likert, R., 565
Lilly, Dave, 302
Lima, L., 569
Lincoln, J. F., 563
Liska, L. Z., 565
Litrenta, Kim, 396
Litterer, J. A., 549
Littman, J., 567
Lizaridis, Mike, 198–199
Locke, Edwin A., 559, 562, 563, 565
Loeb, M., 565
Logan, Don, 337
Lohr, S., 550
Long, J. S., 555
Lorange, P., 561
Loray, Carol, 359
Lorsch, J. W., 548, 560
Lott, Trent, 486
Lovelie, L., 572
Lowrey, Tom, 487
Lowry, Tom, 168, 239
Lublin, J. S., 561, 567, 569, 570
Lublin, Joann S., 573
Luckman, T., 552
Luthans, Fred, 563
Lynthon, Michael, 239
- M**
Maccoby, M., 564
Macintosh, N. B., 570
MacIntyre, A., 552
MacKenzie, S. B., 565
Mackey, John, 355–356, 357
Maden, Omar, 311–313
Magee, Yada, 466
Maguire, Tobey, 238
Mahony, T. A., 548
Makhjani, M. G., 566
Malnight, T. W., 556
Malone, M. S., 570
Mangalindan, Mylene, 573
Mann, Richard A., 125–126, 555
Mannix, E. A., 549
March, J., 557, 570
March, James G., 177, 179
Marcia, J., 561
Marcus, Bernie, 3
Margulies, N., 561
Markels, A., 567
Marra, David, 511
Martell, R. F., 555
Martin, David, 167
Martin, R. A., 562
Martinez, Angela, 334
Martinez, M. N., 552
Mashaba, Herman, 366
Maslow, Abraham H., 329–331, 562
Mason, P. A., 548
Mason, R. O., 558
Mathieu, J. E., 551
Mathis, R. L., 569
Matlack, C., 568

Matta, E., 548
 Mauborgne, Renee, 573
 Maurer, T. J., 562
 Mayer, J. D., 551
 Mayo, Elton, 66, 549
 McAlister, Jon, 453
 McAllister, Jeff, 511, 512
 McCallister, Michael B., 318–319
 McCallum, Daniel, 477
 McCann, J., 548
 McCann, Mary, 334
 McCartney, S., 571
 McClelland, David C., 59, 329, 331–332, 550, 562
 McCool, William, 184
 McCormick, Chris, 201–202
 McCrae, R. R., 550
 McDowell, Mary, 260
 McGee, Liam E., 451–452
 McGee, S., 552
 McGinn, Richard, 241
 McGraw, D., 548
 McGregor, Douglas, 47–48, 549
 McGuire, J., 548
 McGurn, Patrick, 131
 McKay, B., 570
 McKenna, D. D., 548
 McLean, B., 552
 McMahan, G. C., 568
 McMenamin, B., 555
 McNealy, Scott, 179, 180, 182
 Mc Nerney, James, Jr., 37–39
 McWilliams, G., 548
 Mehta, S., 563
 Mercer, Kenneth B., 351
 Meshoulam, I., 568
 Metthee, I., 555
 Michels, A. J., 563
 Miles, R., 560
 Miller, B. C., 567
 Miller, D., 560
 Miller, Jerry, 505
 Miller, Jonathan F., 486–487
 Miller, K., 565, 566
 Milliman, J., 568
 Mills, T. M., 566
 Mintzberg, Henry, 19–20, 24, 548, 564
 Mirguet, Robert, 471
 Mische, Justus, 358
 Mitchell, R., 569
 Mitchell, T. R., 562, 563
 Mitroff, I. I., 558
 Moberg, D. J., 552
 Mobley, W. H., 551
 Mohr, D. C., 552
 Mollenkamp, C., 570
 Monczke, R. M., 555
 Montebello, A. R., 567
 Moody, R. J., 562
 Moore, Gordon, 473
 Moore, Richard H., 130
 Moreno, J., 555
 Moriguchi, Takahiro, 32
 Morse, Jodie, 572
 Morse, N. C., 565
 Morton, M., 561
 Moskowitz, M., 564
 Moss, S. E., 570
 Mottola, Thomas D., 239
 Mount, M. K., 550
 Mouritsen, Russell H., 573
 Mouton, J. S., 565

Mowday, R. T., 563
 Mulcahy, Anne, 281, 289
 Mullaney, T. J., 570
 Muller, Wolfgang, 40
 Mullins, Leo, 443
 Mulvihill, G., 559
 Muris, T., 559
 Murphy, P. E., 553

N

Nabers, W., 570
 Naj, Amal Kumar, 572
 Nakane, C., 556
 Nakarmi, L., 565
 Napier, N. K., 568
 Nardelli, Bob, 4, 5, 6, 12, 23, 24, 302, 307
 Nash, L. L., 553
 Nathan, M., 569
 Nayeri, F., 570
 Near, J. P., 553
 Neill, B., 557
 Nelson, R. R., 570
 Nemetz, P., 571
 Neuijen, B., 556
 Nevijen, Bram, 162
 Newman, B., 570
 Newman, W. H., 561
 Nichols, N. A., 571
 Nicholson, N., 562
 Nickel Anhalt, K., 510
 Niehoff, B. P., 565
 Nierenber, Roger, 368–369
 Nightingale, Deborah, 281
 Nissen, David R., 86
 Nitschke, Dale, 263
 Nixon, Richard M., 187
 Nobuyuki Idei, 239
 Noe, R. A., 550, 569
 Nogues, Thierry, 415
 Nolen, George C., 382
 Nord, W. R., 548
 North, Douglass C., 556
 Nussbaum, B., 567
 Nystrom, L. E., 551
 Nystrom, P. C., 558

O

O'Boyle, T. F., 567
 O'Brian, B., 571
 Obstfeld, M., 556
 Occhifinto, Robert, 31
 O'Connell, P., 558
 Ohayv, Denise Daval, 162, 556
 Ohlott, P. J., 548
 Ohr, George, 190, 191
 Okada, Motoya, 511
 Oldham, G. R., 250–251, 560
 O'Leary-Kelly, A. M., 555
 Oliff, Allen, 198
 Olilla, Jorma, 260
 Olsen, J. P., 557
 Olsen, Ken, 173, 181
 O'Mara, J., 549
 O'Neill, Patrick J., 384
 O'Neill, Susan, 573
 O'Reilly, B., 571
 O'Reilly, C. A., 570
 Organ, D. W., 548, 549
 Ortega, B., 552, 572
 Ostrom, T. M., 568
 Otellini, Paul S., 416–417
 Ouchi, William G., 561
 Overholt, A., 571
 Overman, S., 568

P

Packard, David, 79–80, 313, 468
 Paetzold, R. L., 555
 Paez, B. L., 559
 Page, R. C., 548
 Palmeri, Christopher, 135, 559
 Palmisano, Samuel J., 56–57, 79, 550
 Palrecha, R., 564
 Panzer, K., 548
 Papademetriou, Demetrios G., 133
 Pape, W. R., 567
 Parahalad, C. K., 559
 Park, A., 486
 Parker, L. D., 549
 Parker, S. R., 548
 Parson, Bill, 184
 Parson, Richard S., 486
 Parsons, Richard "Dick," 336–337, 563
 Patterson, A., 555
 Paull, Matthew, 264, 265
 Pearce, J. A., 552
 Pearce, J. A., II, 559, 567
 Pechman, Marsha J., 351, 353
 Pedigo, P. R., 548
 Peiperl, M. A., 569
 Pellet, J., 548
 Pennings, J. M., 548
 Penrose, E., 559
 Perez, Antonio M., 279–280
 Perlez, J., 556
 Perrow, Charles, 246, 549, 560
 Perry, M. K., 559
 Peters, L. H., 554, 565, 569
 Peters, T., 571
 Peterson, George C., 238
 Peterson, R. S., 551
 Petty, R. E., 568
 Pfeffer, Jeffrey, 176, 557, 561, 564
 Phelps, R., 559
 Pickering, J. F., 571
 Pillai, R., 566
 Pirtle, Thomas, 466
 Pischetsrieder, Bernd, 237–238
 Podaskoff, P. M., 565
 Poernomo, Ardian, 453
 Pohlmann, J. T., 565
 Polzer, J. T., 553
 Pondy, L. R., 570
 Poniewozik, J., 554
 Poretto, J., 566
 Porter, C. O. L. H., 550
 Porter, E., 569
 Porter, Lyman W., 66, 563
 Porter, Michael E., 216, 226–227, 229, 555, 556, 559, 560, 570, 571
 Poteet, M. L., 569
 Poulsen, Henrik, 259
 Pounds, S., 562
 Prabham, Bassad, 427
 Prahalad, C. K., 559

Premack, S., 570
 Pritchard, R. D., 562
 Provitera, M. J., 548
 Pugh, D. S., 561
 Pulienthuruthel, J., 453

Q

Quinn, J. B., 568

R

Radosevich, D. J., 563
 Raia, A. P., 561
 Rairhurst, T. 489n
 Ramanujam, V., 559
 Ramirez, George, 32
 Ramon, Ilan, 184
 Randel, A. R., 549
 Ratz, J. M., 554
 Rauch, Maggie, 573
 Raven, B., 564
 Ravlin, E. C., 567
 Rayasam, R., 564
 Rebello, J., 565
 Redstone, Sumner, 255–256
 Reeves, M., 567
 Regan, M. B., 570
 Reich, Robert B., 141, 555, 556
 Reimer, E., 565
 Reinert, P., 558
 Reinhardt, A., 560
 Rhode, J. G., 561
 Rice, F., 558
 Rich, E., 571
 Richie, Roy, 425
 Richie, Susan, 334
 Rider, Michael, 395
 Riedman, Benjean, 387
 Ritter, Mike, 301
 Roach, Andy, 464
 Robbins, S., 564
 Roberts, Barry S., 125–126, 555
 Roberts, Dexter, 169, 238
 Roberts, J. L., 563
 Roberts, Mike, 264, 265
 Robertson, I., 572
 Robinson, B., 68
 Robinson, G., 549, 555
 Roddick, Anita, 56
 Rodgers, R., 561
 Rodgers, T. J., 300, 478
 Rodriguez, Cesar, 122
 Rodriguez, L., 555
 Rodriguez, Ray, 135
 Roethlisberger, F. J., 46–47
 Rogers, E. M., 570
 Rokeach, Milton, 60–62, 550
 Romano, Frank J., 280
 Ronen, S., 562
 Roos, D., 560
 Rose, R. L., 564
 Rosen, B., 555, 567
 Rosen, Leonard G., 199
 Rosenfeld, J., 565
 Ross, G. H. B., 561
 Ross, T. L., 563
 Rosseau, D. M., 572
 Roth, D., 564
 Rotter, J. B., 550
 Roukis, Steve, 87

Rowley, I., 512
 Roy, D., 549
 Ruderman, M. N., 548
 Rugman, A. M., 556
 Rumbaut, Ruben G., 134
 Rumelt, R. P., 559
 Russo, J. E., 558
 Russo, Patricia, 9, 10, 11, 11f, 24, 242
 Ryan, Kevin, 445
 Rynes, S. L., 555, 569

S

Saari, L. M., 563
 Salamon, J., 569
 Salovey, P., 551
 Salpukas, A., 571
 Salter, C., 572
 Sanchez, J. I., 570
 Sanchez, Maria, 332–333
 Sanders, G., 162, 556
 Sanders, L., 559
 Sawyer, J. E., 558
 Sayeed, L., 567
 Scandura, T. A., 572
 Scanlon, Joseph, 344–345
 Scannell, Peter, 62
 Schacter, S., 567
 Schaffer, Robert H., 382–383
 Schaht, Henry, 241–242
 Schares, G. E., 566
 Schaubroeck, J., 552
 Scheffman, D., 559
 Schein, H., 552
 Schendel, D., 559
 Schiller, Z., 550
 Schlosser, J., 564
 Schmalensee, R., 556, 559
 Schmidt, K. A., 558
 Schmitt, R. B., 570
 Schneider, Benjamin, 71–72, 551, 552, 564
 Schoemaker, P. J. H., 558, 559
 Schoenfeldt, L. F., 563, 568
 Schoenherr, R. A., 560
 Schonfeld, Erik, 573
 Schreisheim, C. A., 565, 566
 Schreyogg, G., 561
 Schuler, R. S., 569
 Schulmeyer, Gerhard, 39
 Schulz, J. W., 561
 Schuman, M., 565
 Schumpeter, Joseph, 556
 Schwartz, J., 558
 Schwenk, C. R., 558
 Scoble, Robert, 486
 Scott, W. R., 570
 Sculley, John, 26
 Segal, T., 555
 Seiders, K., 549
 Sellers, P., 548, 565
 Seltzer, J., 566
 Semier, Ricardi, 419–420
 Semler, R., 568
 Senge, Peter M., 181–182, 188, 189, 557, 558
 Senkbiel, Liz, 402
 Serwer, A., 566
 Seyle, D. C., 553
 Shallenbarger, S., 570
 Shama, A., 549

Sharpe, R., 553, 569
 Shaw, J. B., 563, 568
 Shaw, K. N., 563
 Shaw, M. E., 566
 Shaw, W. H., 549, 552
 Shellenbarger, S., 569
 Shepperd, J. A., 568
 Sherman, S., 556
 Shinal, J., 559, 560
 Shleifer, A., 559
 Shoda, Masafumi, 511
 Shook, D., 558
 Shope Griffin, N., 572
 Siegel, Eric, 172
 Siegel, Steven, 67
 Simmering, M. J., 550
 Simon, Herbert A., 177, 179, 557
 Simons, J., 559
 Simons, R., 561
 Sinclair, R. C., 551
 Singer, B., 555
 Skill, M. S., 548
 Skinner, B. F., 338, 563
 Skinner, James A. "Jim," 264, 265
 Slate, E., 551
 Slaughter, J. E., 552
 Sloan, Allan, 573
 Slump, David J., 86–87
 Smith, D. B., 551, 564
 Smith, David, 480
 Smith, F. J., 66
 Smith, Fred, 257
 Smith, Russell, 9, 552
 Smutniak, J., 557
 Smyjunas, Robert, 84
 Snell, S. A., 569
 Sohn, Adam, 486
 Solomon, R. C., 553
 Solomon, Steve, 215
 Sommerville, R. B., 551
 Song, L., 70
 Sorcher, M., 563
 Spalding, Carl, 108
 Spangler, W. D., 550, 562, 564
 Spector, P., 550
 Spiller, P., 559
 Spitzer, Eliot, 59, 129–130
 Sproul, J. R., 569
 Sproull, L. S., 567
 Stahl, M. J., 550, 562
 Stalk, G., 570, 572
 Stalker, G. R., 560
 Stamps, D., 554
 Stanley, Terri Patsos, 21–22, 24
 Starbuck, W. H., 558
 Stavrika, C., 553
 Staw, B. M., 551, 553, 565, 571
 Steers, R. M., 563
 Stein, N., 562
 Steinberg, John, 334
 Steiner, Gregg, 63
 Steinhafel, Gregg, 263
 Steinmann, H., 561
 Stemple, J., 549
 Stengel, James R., 167
 Stern, Edward J., 59
 Stern, G., 550
 Stevens, A., 555
 Stewart, R., 548

Stewart, T. A., 564, 566
 Stogdill, R., II, 569
 Stogdill, R. M., 564
 Stone, A., 552
 Stone, B., 562
 Stoner, J. A. F., 572
 Stopford, J., 560
 Stracker, Karen, 470
 Strauss, S. G., 567
 Stroebe, W., 558
 Strutt, A., 568
 Stundza, T., 572
 Sullivan, Martin J., 130
 Sullivan, R. L., 569
 Sullivan, S. E., 549, 572
 Sung, J., 564
 Suro, Roberto, 133
 Sutcliffe, K. M., 549
 Swann, W. B., Jr., 553
 Swartz, Jon, 573
 Swartz, M., 552

T

Tashiro, H., 568
 Tata, Mark, 445
 Taylor, Frederick W., 41–43, 46, 549, 560
 Taylor, S. E., 555
 Teece, D. J., 559
 Tellegen, A., 551
 Tenbrunsel, A. E., 552
 Tepper, B. J., 565
 Terhune, C., 570
 Tetrault, L. A., 565
 Tett, R. P., 550
 Thacker, R., 555
 Tharenou, P., 549
 Thomas, Cathy Booth, 573
 Thomas, David A., 435
 Thompson, J. D., 561
 Thurston, K., 569
 Tierney, C., 556
 Tindell, Kip, 349–350
 Tiplady, Rachel, 280, 568
 Tischler, Linda, 374, 566, 573
 Tkaczyk, C., 549
 Tobin, D. R., 549
 Todd, P. A., 570
 Tomiki, Hisashi, 504
 Tosi, H. L., 561, 563
 Totty, M., 570
 Townsend, A. M., 567
 Trent, R. J., 555
 Trevino, L. K., 552, 553, 571
 Triandis, H. C., 562
 Trice, H. M., 551, 552
 Troy, M., 556
 Tubbs, M. E., 563
 Tuckman, B. W., 567
 Turban, E., 570, 571
 Turner, C., 561
 Tversy, Amos, 175
 Tylor, Edward B., 556
 Tyson, Lynn, 434

U

Uchitelle, L., 570
 Ulrich, Robert, 263

V

Valian, Virginia, 120, 555
 Van Der Beek, R., 568
 Van Fleet, D. D., 565, 566
 Van Maanen, J., 552, 553, 561
 van Scherpenberg, Jens, 39
 Vann, M., 555
 Vaquero, Carlos, 132
 Varadarajan, P., 559
 Vardi, N., 549
 Vaughn, S., 554
 Velasquez, Carlos, 131–132
 Velasquez, Maria, 131–132, 552
 Vickers, M., 131
 Victor, B., 553
 Vishny, R. W., 559
 Vitzhum, C., 560
 Von Glinow, M., 569
 von Pierer, Heinrich, 39–40, 371–372, 373, 381–383
 Vroom, Victor H., 324

W

Wack, P., 559
 Wald, M. L., 558
 Waldman, D. A., 566
 Wall, T. D., 66, 548, 567
 Waller, M. J., 548
 Walster, W. G., 558
 Warkentin, M. E., 567
 Warner, M., 558
 Warr, P. B., 66
 Warren, E. K., 572
 Washko, John, 435
 Watanabe, Katsuki, 509–510
 Waterman, A. S., 553
 Waterman, R. H., Jr., 571
 Watkins, S., 552
 Watson, D., 551, 558
 Waxer, Cindy, 573
 Weaver, Amy, 387
 Weber, J., 555
 Weber, Max, 43–45, 549
 Webster, J., 68
 Weick, K. E., 552, 561
 Weinberg, A., 550
 Weinberger, David, 485
 Weiner, S. P., 567
 Weintraub, Arlene, 135
 Weiss, H. W., 562, 563
 Welch, Jack, 37, 85, 86, 96, 206, 294, 360, 383, 421
 Wellington, Sheila, 111, 553
 Wells, L., 560
 Wells, Paul A., 351
 Wessel, D., 569
 West, M. S., 554
 Wexley, K. N., 569
 Wheeler, J. A., 569
 Wheeler, J. V., 548
 Wheeler, S. R., 554
 Wheelwright, Stephen C., 557, 571
 Whitely, W., 572
 Whiting, V., 549, 572
 Whitman, Margaret C. "Meg," 317–318
 Williams, E. S., 566
 Williams, J. R., 559

Williams, K., 568
 Williams, M. L., 565, 571
 Williams, O. E., 571
 Willig, R. D., 556, 559
 Winer, Dave, 485
 Winslow, R., 570
 Winter, D. C., 550, 562
 Winter, R. R., 556
 Winter, S. G., 556
 Witt, L. A., 550
 Wofford, J. C., 565
 Womack, J. P., 560
 Wong, C., 70
 Woodman, R. W., 558

Woodward, Joan, 246–247, 560
 Woolridge, B., 561
 Woycke, J., 550, 562
 Wozniak, Steve, 25
 Wren, D., 549
 Wright, P. M., 569
 Wysocki, B., 548

Y

Yamada, Tadataka “Tachi,”
 197–198, 360
 Yang, Catherine, 487

Yang Ki In, 168
 Young, S. M., 559, 572
 Youngblood, S. A., 554, 569
 Yukl, G., 564, 565, 566

Z

Zachary, G. P., 570
 Zager, R., 563
 Zajac, D. M., 551
 Zan, M., 110
 Zander, A., 567
 Zanna, M., 551

Zarb, Frank G., 130
 Zawacki, R. A., 561
 Zeldes, Nathan, 472
 Zeller, W., 563
 Zellner, Wendy, 558, 564, 573
 Zhou, J., 551
 Zicker, M. J., 552
 Ziegler, B., 571
 Zuckerman, H., 555

Subjects

A

Ability selection tests, 430, 431
 Accomplishment, and
 motivation, 323
 Accuracy in effective plans, 208
 Achievement
 and motivation, 323
 needs for, McClelland's,
 59–60, 331–332
 orientation toward, 163, 368
 Action
 goal-setting theory of
 motivation, 336
 managerial functions, 8–9, 12, 15
 organizational culture, 78–80
 Activity ratio, 292, 293
Ad hoc committee, 271, 395
 Adaptive culture, 305–307
 Adding value, 226, 231
 Adjourning, self-managed work
 teams, 401
 Administration
 bureaucratic theory, Weber's,
 43–45
 decision making model,
 177–179
 Advertising in spokesperson
 managerial role, 20, 21
 Affiliation needs, McClelland's,
 59–60, 331–332
 African Americans, in diverse
 workplace, 109–110,
 112–113
 Age Discrimination in
 Employment Act (1967),
 111, 424
 Age issues, 110, 152, 423–424
 Agreeableness, 54, 55–56
 AI (artificial intelligence),
 475, 480
 AIDS, 115–116, 425
 Alaska Natives, in diverse
 workplace, 112
 Alliances, strategic, 222, 224,
 272–275
 Alternatives
 administrative decision-making
 model, 178–179
 decision-making process, 181–185

Ambiguous information,
 administrative decision-
 making model, 178, 179
 American Federation of Labor-
 Congress of Industrial
 Organizations
 (AFL-CIO), 446
 American Indians, in diverse
 workplace, 112
*American Journal of Public
 Health*, 119
 Americans with Disabilities Act
 (1990), 111, 114, 424
 Annual meeting, company,
 76–77
 Answering machines, 470
 Applications software, 475
 Apprenticeship, 432
 Artificial intelligence (AI),
 475, 480
 ASA (attraction-selection-attribution)
 framework, 71–72, 74
 Asians, in diverse workplace,
 112–113
 Assessment centers, selection,
 430, 431
 Assessment of need, 308–309
 Assets, financial performance
 measure, 292–293
 Asynchronous technologies, 397
 Attitude, 62–66
 defined, 60, 62
 job satisfaction, 63–65
 organizational commitment,
 65–66
 organizational culture, 73
 Attraction-selection-attribution (ASA)
 framework, 71–72, 74
 Attractiveness, as diversity issue, 118
 Authority
 allocation of, organizational
 design, 264–268
 in bureaucratic theory, Weber's,
 43–44
 centralization of, 267–268
 decentralized, 247–248
 defined, 264
 Follett on, 45
 hierarchy of, 264–267
 organizational environment, 243

Autonomy, job characteristics
 model, 250, 251

B

Background information, human
 resources, 429–430
 Backward vertical integration, 225
 Balance, conformity vs. deviance,
 403–404
 Bargaining, supplier, 140–141
 Barriers
 to entry, 146–147
 to trade, 154, 155–159
 B2B (business-to-business)
 network, 272–275
 Behavior control, 298–303
 bureaucratic control, 300–303
 defined, 289–290
 direct supervision, 298–299
 management by objectives
 (MBO), 299–300
 organizational change, 307
 organizational control, 291,
 298–303
 organizational culture, 303
 Behavior model, leaders and
 leadership, 363–364
 Behavior performance
 appraisal, 437
 Belongingness needs, Maslow's,
 329, 330
 Benchmarking, 311
 Benefits, human resources, 423,
 441, 444
 Bias and diversity, 109
 Big Five personality traits, 52–58
 Blogging, 485–486
 Body language, 465–466
 Body weight, as diversity issue,
 118–119
 Bonus plans, 343–344
 Bottom-up change, 310
 Boundaryless organization, 275
 Bounded rationality, administrative
 decision-making model, 177
 Brainstorming, 192
 Brand loyalty, 147
 Brand name, retailer, 230
 Brevity in managerial life, 23

Budgets, operating, 295
 Bureaucracy, 43–44
 Bureaucratic control, 300–303
 Bureaucratic theory, Weber's,
 43–45
 Business, defined, 209
 Business-level plan, 203–206
 Business-level strategy
 defined, 204
 differentiation strategy, 9,
 227–231, 232
 focused, 230–231
 formulation, 204, 213, 226–231
 low-cost, 9, 227, 229–231, 232
 organizational goals, 294
 time horizons, 206
 Business-to-business (B2B)
 network, 272–275
Business Week; see also Cases for
 discussion
 AIG ethics, 129–131
 Albertsons leadership, 383–384
 AOL rebound, 486–487
 Bank of America (BoFA) human
 resources, 451–452
 BlackBerry, 198–199
 Boeing gender discrimination,
 350–353
 eBay organizational control,
 317–318
 GE leadership and culture
 changes, 85–87
 gender and pay at Boeing,
 350–353
 global environment, 167–169
 Google employee talent, 453
 Hispanic business, 131–135
 human resources, 451–453
 Humana restructuring, 318–319
 information technology (IT), 24
 Intel reorganizations, 416–417
 Jingle Jim's International
 Market, 83–85
 Kodak restructuring, 279–280
 mass market changes, 167–169
 Microsoft employee blogging,
 485–486
 organizational design, 279–281
 Posco steel in South Korea,
 168–169

BusinessWeek—Cont.

- Siemens revitalization, 39–40, 381–383
- strategy formulation, 237–239
- 3M leadership, 37–39
- Volkswagen, 237–238
- Wal-Mart competition, 83–85
- Xerox restructuring, 280–281

C

- Cafeteria-style benefit plans, 444
- Canada, NAFTA, 154, 159–160
- Cannabis, ethics of, 92–93
- Capabilities and diversity, 114–116
- Cases for discussion; *see also BusinessWeek*; Video cases
 - decision making, 197–199
 - diversity, 131–135
 - ethics, 129–131
 - global environment, 167–169
 - groups and teams, 415–417
 - human resources, 451–453
 - leaders and leadership, 381–384
 - management process, overview, 37–40
 - managers, personal characteristics of, 83–87
 - motivation, 349–353
 - operations management, 508–512
 - organizational control, 317–319
 - organizational design, 279–281
 - personal characteristics of managers, 83–87
 - strategy formulation, 237–239
- Centralization of authority, 267–268
- CEOs (chief executive officers), 14–15, 442–443
- Ceremonies, 76–78
- Chain of command, minimum, 267
- Challenger* space shuttle disaster (1986), 173, 182–184, 187, 523–524
- Change
 - ethics, 92–93
 - global environment, 154–164
 - managerial roles, 16–19
 - rapid pace of global, 27
 - technological, 149–150
- Characteristics of managers; *see* Managers, personal characteristics of
- Charismatic leadership, 372
- Chief executive officers (CEOs), 14–15, 442–443
- Chief operating officers (COOs), 14–15
- Childcare, 116–117
- China, 16, 509–510
- Choice among alternatives, decision-making process, 184–185
- Civil Rights Act (1964, 1991), 111, 423, 424
- Clan control, 291, 303–307
- Classical decision-making model, 176–177
- Classroom instruction, 432–433



- Client-appraisals, performance, 438–439
- Clients, computer networks, 474, 475
- Coercive power, 360
- Cohesiveness, group dynamics, 405–408
- Collective bargaining, 447
- Collectivism, 161–162, 358
- Columbia* space shuttle disaster (2003), 183, 184, 523–524
- Command groups, 395
- Commission pay, 344
- Communication, 454–487
 - dangers of ineffective, 466–467
 - defined, 462
 - electronically transmitted spoken, 469–470
 - face-to-face, 467, 468–469, 470, 481
 - group participation, 406
 - impersonal written communication, 467, 471–472
 - importance of good, 463
 - information and the manager's job, 457–462
 - information richness, 467–468, 480–481
 - Information Technology: collaboration software and teams, 464
 - Information Technology: e-stores, 460
 - Information Technology: Intel's 10 Commandments of Email, 472
 - information technology limitations, 480–481
 - information technology revolution, 473–476
 - management information systems, 476–480
 - Management Snapshot: Herman Miller, 455–456
 - Manager as Person: Lewent at Merck, 479–480
 - media for, 467–472
 - organizational hierarchy, 266–267
 - personally addressed written communication, 467, 470–471
 - process of, 464–466
 - sexual harassment policy, 125
 - spoken communication, 465–466, 467, 469–470
 - verbal communication, 465–466, 469–470
 - wireless, 473–474
 - written, 470–472
- Community, as ethical stakeholder, 97–99
- Competencies, 25
- Competition
 - five forces model, 216
 - managerial hierarchy changes, 16–17
 - organizational control, 286
 - rapid pace of change, 27
 - task environment, 148
- Competitive advantage; *see also* Strategy formulation
 - Competitive advantage—*Cont.* components, 285
 - customers and customer responsiveness, 28, 29, 285, 286
 - defined, 28
 - global challenges, 28–30
 - good communication, 463
 - groups and teams, 389
 - human resource management (HRM), 421
 - operations management, 490–491
 - strategy formulation, 232
- Competitors, 139, 146–148
- Completeness of information, 459
- Complexity
 - of integrating mechanism, 270
 - of mental models, 189
 - of technology, 246, 290
- Computer networks, 474–475
- Conceptual managerial skills, 23–24, 25
- Concurrent controls, 288
- Conformity, group dynamics, 402–407
- Conscientiousness, 54, 56
- Consideration, behavior model, 363
- Context
 - Fiedler's contingency model, 366–367
 - leader substitutes model, 369–370
- Contingency models of leadership, 365–370
 - defined, 365
 - Fiedler's, 365–367, 370
 - leaders substitutes model, 369–370
 - path-goal theory, House's, 367–369, 370
- Contingency planning, 208–209
- Contingency theory, 243
- Continuous-process technology, 247
- Continuity in effective plans, 208
- Control; *see also* Organizational control
 - authority allocation, 264–265
 - behavior control, 298–303
 - external locus of, 59
 - of information, 461–462
 - internal locus of, 58
 - organizational culture, 79
 - organizational systems, 287–288
 - planning importance, 208
 - process of organizational, 288–292
- Control systems, 287–288
- Controlling, 8, 12–13, 15, 285
- Conversion, control systems, 287–288
- Conversion stage, production system, 491
- Coordination
 - of information, 462
 - organizational design, 264–272
 - planning importance, 208

- COOs (chief operating officers), 14–15
- Corporate-level plan, 203–206, 289, 309–310
- Corporate-level strategy
 - defined, 204
 - formulation, 204, 213, 217–226
 - international expansion, 219–225
 - single business concentration, 217–218
 - time horizons, 206
 - vertical integration, 225–226
- Corrective action, control process, 290–291
- Cost
 - administrative decision-making model, 178–179
 - focused low-cost strategy, 230
 - human cost of productivity improvements, 504–505
 - low-cost business-level strategy, 9, 227, 229–231, 232
 - operating budgets, 295
 - tall organizational hierarchy, 267
 - of technology, 473
- Creativity, 189–194, 376
- Critical thinking and negative mood, 68
- CRM (customer relationship management), 18, 493–494
- Cross-departmental responsibility, 14, 16
- Cross-functionality
 - diversity, 118–119
 - Follett on, 45
 - groups and teams, 262, 270–272, 391, 394, 401
- Cross-training, 28
- Culture; *see also* Organizational culture
 - as a barrier, 156–157
 - cross-cultural teams, 394
 - global environment, 156–157, 160–164
 - leadership styles, 358
 - national, 145, 160–164
 - need theories, 330–331
 - organizational change, 310
- Current ratio, 292, 293
- Customer relationship management (CRM), 18, 493–494
- Customers, defined, 144
- Customers and customer responsiveness
 - business defined, 209
 - competitive advantage, 28, 29, 285, 286
 - control process, 288
 - e-commerce, 157–158
 - as ethical stakeholders, 94, 97
 - five forces model, 216
 - global environment, 144–145
 - good communication, 463
 - by groups and teams, 389, 391
 - operations management, 490–494

- Customers and customer responsiveness—*Cont.*
task environment, 139, 144–146
vertical integration, 225–226
- D**
- Dangers of ineffective communication, 466–467
- Data, 457; *see also* Information and the manager's job
- Days sales outstanding, 292, 293
- Debt, financial performance measure, 292–293
- Debt-to-assets ratio, 292, 293
- Decentralization of authority, 267–268, 299
- Decentralized authority, 247–248
- Decision making, 170–199
administrative model, 177–179
cases for discussion, 197–199
classical model, 176–177
creativity, 190–194
defined, 173
Diversity Focus: alternative questions and answers, 190–191
ethical rules, 99–102
Ethics in Action: NASA's organizational culture, 183–184
group decision making, 185–188
hierarchy of authority, 264–265
and information, 461
Management Snapshot: ABS decisions, 171–172
Manager as Person:
overconfidence, 175–176
nature of managerial, 172–179
nonprogrammed, 174–176, 179–180, 478
organizational change, 309–310
organizational learning, 188–190
programmed, 173–174
steps in process, 179–185
summary and exercises, 194–197
- Decision-making process, 179–185
alternatives, 181–185
choice among alternatives, 184–185
evaluation of alternatives, 182–183
feedback, 185
generation of alternatives, 181–182
implementation of alternatives, 185
models for, 179–180
recognize need for decision, 180–181
- Decision support systems, information technology, 478–479
- Decisional managerial roles, 20–21, 120
- Decoding, communication process, 465
- Delphi technique, 193
- Demand forecasting, 425
- Demographic forces, general
global environment, 139, 151–152
- Department, 13, 14, 16, 270, 395
- Deregulation, 152
- Design of organizational structure; *see* Organizational design
- Development, human resources, 421, 422, 423, 432, 434–436
- Developmental consideration, 373
- Deviance in group dynamics, 402–405
- Devil's advocacy, 68, 188
- Differentiation, business-level strategy, 9, 227–231, 232
- Difficulty of goals, 294, 335–337
- Dilemmas, ethical, 91, 100, 101
- Direct contact, as integrating mechanism, 270
- Direct supervision, behavior control, 298–299
- Direction of behavior, and motivation, 322
- Directive behavior, path-goal theory, 368
- Disabilities and diversity, 114–116, 423–424
- Discrimination, 109
- Disseminator managerial role, 20, 22, 120
- Distance as a barrier, global environment, 156–157
- Distortion of information, 477
- Distributors
defined, 143
as ethical stakeholders, 94, 97
ethics, 97, 98
global environment, 143–144
task environment, 139, 143–144
- Disturbance handler managerial role, 20, 21, 120
- Diversification, 218–219
- Diversity, 109–126
age, 110
capabilities, 114–116
cases for discussion, 131–135
critical managerial roles, 119–121
cross-functionality, 118–119
decision making, 188
defined, 109
disabilities, 114–116
effective management, 121–123
gender, 110–112
Global Managing: Asians and Hispanic population growth, 112–113
global workforce challenges, 31–32
group dynamics, 407
management of, 119–123
Manager as Person: business creation and determination, 121–122
managing, 90
race and ethnicity, 112–114
reasons to study, 109–110
religion, 114
sexual harassment, 124–126
sexual orientation (gay/lesbian), 117–118
socioeconomic background, 116–117
summary and exercises, 126–129
top-management teams, 394
- Diversity Focus
alternative questions and answers, decision making, 190–191
balanced life and organizational commitment, 63
employee wellness benefits, 444–445
gays and lesbians in workplace, 117–118
human resources, 434–435, 444–445
mentoring, 434–435
motivation, 328–329, 336–337
Nike diverse customer appeal, 328–329
Time Warner turnaround, 336–337
Tower Automotive leadership, 375–376
Union Bank of California competitive advantage, 31–32
- Division, defined, 203
- Division of labor, 248–249, 399
- Divisional managers, 203, 294
- Divisional structure
coordinating, 264–272
defined, 254
geographic structure, 254–255, 257–260
hybrid structure, 262–263
market structure, 254–255, 260
matrix structure, 260–262
organizational change, 310
organizational design, 254–260, 264–272
product structure, 255–257
product team structure, 261, 262
- Dominance, trait model, 362
- Dot-com industry
competition, 146
distributors, 143
e-commerce, 33, 157–158
economic forces, 149
economies of scale, 147
equity theory, 335
general environment, 148
goal setting, 211
leadership, 358
merit pay, 344
organizational structure, 267
suppliers, 140
- Downsizing, 16
- Duration; *see* Time issues
- E**
- E-commerce, 33, 157–158; *see also* Dot-com industry
- Economic feasibility, decision making, 182
- Economic forces, general global environment, 139, 149
- Economies of scale, 146–147
- Education, human resources, 421–423, 432–434, 435
- EEO (equal employment opportunity) laws, 423–424, 430
- Effectiveness
communication, 466–467
control systems, 287
defined, 5–6
diversity, 109, 121–123
empowerment, 361–362
ethical behavior, 102–104
functional structure, 253
gender, 375
and information, 461
minimum chain of command, 267
organizational control, 286
organizational groups and teams, 388–393
and performance, 6
of plan, 208
reward power, 360–361
self-managed work teams, 396
- Efficiency
bureaucratic theory, Weber's, 43–45
competitive advantage, 28, 285
control process, 288–289
customers, responsiveness to, 490
defined, 5, 490
ethical behavior, 102–104
facilities layout, 496–500
flexible manufacturing layout, 496, 498–501
functional structure, 253
good communication, 463
just-in-time inventory, 501–502
operations management improvements, 490, 495–504
outsourcing, 16
and performance, 6
process reengineering, 502–503
self-managed work teams, 502
- Effort, 322, 325, 327
- Electronic trail, communication media, 468
- Electronically transmitted spoken communication, 469–470
- Email, 470–471, 472
- Emotional intelligence, 68–70, 73, 376
- Emotions
defined, 67
of managers, 60, 67–68
organizational culture, 73
punishment, operant conditioning, 340
- Employee stock options, 343–344
- Employees and workers; *see also* Groups and teams; Human resources (HR); Job analysis
blogging, 485–486
competitive advantage, 29
decentralization of authority, 267–268
with disabilities, 114–116
disseminator managerial role, 20, 21
diversity, 31–32
division of labor, 248–249
empowerment, 17, 29, 249
as ethical stakeholders, 94, 96
ethics, 96
Follett on management of, 45
Hawthorne effect, 46–47

- Employees and workers—*Cont.*
 job characteristics model, 250–251
 job enlargement and enrichment, 249–250
 job grouping structure, 251–264
 matrix structure, 260–262
 organizational commitment, 63, 65–66
 outsourcing, 16–17
 restructuring, 16–17
 self-managed work teams, 17, 18, 370
 Theory X and Y, McGregor's, 47–48
 total quality management (TQM), 29
 unions and labor relations, 445–447
 workers' compensation, 444
 Employment Act (1967), 111
 Empowerment
 competitive advantage, 29
 defined, 17, 361
 job organizational design, 249
 leader substitutes model, 370
 leadership, 361–362
 Encoding, communication process, 465
 Energy, trait model, 362
 Enhancement
 of performance, 389–391
 rites of, 76, 77
 Enlargement, job, 249
 Enrichment, job, 249–250
 Entrepreneur managerial role, 20, 21, 120
 Entrepreneurs, 311
 Entrepreneurship, 311–313
 Entry
 barriers to, 146–147
 five forces model, 216
 Environment; *see also* Global environment
 external environment, 20, 172–173
 hostile work environment sexual harassment, 124
 internal environment, 20
 international expansion, 221–222
 organizational, 138–139, 243–244
 task environment, 139, 140–146, 148
 Equal Employment Opportunity Commission (EEOC), 423
 Equal employment opportunity (EEO) laws, 423–424, 430
 Equal Pay Act (1963), 111, 424, 445
 Equation for motivation, 324
 Equity, 332–333
 Equity restoration, 333–335
 Equity theory of motivation, 332–335
 defined, 332
 equity, 332–333
 equity restoration, 333–335
 inequity, 333
 pay, 342
 Esteem needs, Maslow's, 329, 330
 Ethical dilemmas, 91, 100, 101
 Ethics, 89–109
 cases for discussion, 129–131
 changes over time, 92–93
 community, society and nation, 97–99
 customers, 97
 decision making, 182–183
 decision-making rules, 99–102
 defined, 91
 distributors, 97, 98
 employees, 96
 ethical dilemmas, 91
 Ethics in Action: Johnson & Johnson, 107, 108–109
 individual, 105, 106
 justice decision-making rules, 100, 101
 and the law, 91–92
 Management Snapshot: Codes of Ethics strengthening, 89–90
 managers, 95–96, 102–104
 moral rights decision-making rules, 100–101
 nature of, 91–93
 operations management, 504–505
 organizational cultures, 106–109
 practical decision-making rules, 100, 101–102
 professional, 105–106
 sexual harassment, 124–126
 societal, 104–105
 sources of organizational, 104–106
 stakeholders, 90, 94–108
 standards, global, 30
 stockholders, 94–95
 summary and exercises, 126–129
 suppliers, 97, 98
 unethical behavior, 102–104
 utilitarian decision-making rules, 99–100
 Ethics in Action
 CEO compensation, 443
 decision making, 183–184
 FDA and diet supplements, 30–31
 honesty, 62
 human cost of productivity improvements, 504–505
 human resources, 443
 Johnson & Johnson, 107, 108–109
 management process, overview, 30–31
 NASA's organizational culture, 183–184
 operations management, 504–505
 organizational design, 274–275
 personal characteristics of managers, 58–59, 62
 sweatshops and shoe manufacturing, 274–275
 whistleblowers, 58–59, 62
 Ethics ombudsman, 106
 Ethnicity and diversity, 112–114, 423–424
 Europe, 150, 155–156
 Evaluation
 of alternatives, decision-making process, 181, 182–183
 organizational change, 310–311
 Executive compensation, 96;
see also Pay
 Expectancy, 325, 328
 Expectancy theory of motivation, 324–329
 defined, 324
 expectancy, 325, 328
 instrumentality, 325, 327, 328
 pay, 342
 valence, 325, 327, 328
 Expense operating budgets, 295
 Experience, openness to, as personality trait, 54, 56
 Expert power, 360–361
 Expert systems, information technology, 480
 Expertise, trait model, 362
 Exporting, international expansion, 222
 External environment, 20, 172–173
 External locus of control, 59
 External recruiting, human resources, 428–429
 Extinction, operant conditioning, 339
 Extraversion, 53–54, 67
 Extrinsically motivated behavior, 323
F
 Face-to-face communication, 467, 468–469, 470, 481
 Facilities layout, 496–500
 Family and Medical Leave Act (1993), 111, 424
 Feedback
 control of, 287, 288
 decision-making process, 181, 185
 goal-setting theory of motivation, 336
 job characteristics model, 250, 251
 phase of, communication, 464
 Feedforward control, 287, 288
 Fiedler's contingency models, 365–367, 370
 Figurehead managerial role, 20, 22, 65, 120
 Financial performance metrics, output control, 292–293
 First-line managers (supervisors), 13, 14, 15–17, 438
 Five forces model, Porter's, 216
 Fixed-position layout, 497–498
 Flat organizational hierarchy, 266–267
 Flexibility, 28, 29, 208, 244
 Flexible manufacturing, 496, 498–501
 Focused business-level strategy, 230–231
 Focused differentiation strategy, 230
 Focused low-cost strategy, 230
 Folkways, 160–161
 For-profit organizations, 16–17, 149; *see also specific companies* [in company index]
 Forecasting, human resources, 425
 Formal appraisal, 440
 Formal education as training, 435
 Formal groups, 394
 Forming, self-managed work teams, 400, 401
Fortune, 24
 Forward vertical integration, 225
 Founder values, 74
 Fragmentation in managerial life, 23
 Franchising, international expansion, 222, 223–224
 Free trade, 154–159
 Free-trade doctrine, 156
 Friendship groups, 398
 Function, defined, 205
 Functional-level plan, 203–206
 Functional-level strategy
 defined, 205, 231
 formulation, 205, 213, 231–232
 international expansion, 219–225
 time horizons, 206
 Functional managers, 205
 Functional structure, 252–253
 Functions, managerial, 7–13
 controlling, 8, 12–13, 15
 defined, 13
 leading, 8, 12, 15
 in matrix structure, 260–262
 organizational design coordination, 264–272
 organizing, 8, 11–12, 15
 overview, 7–8
 planning, 8–10, 15, 206
G
 GATT (General Agreement on Tariffs and Trade), 154, 156
 Gender
 diversity, 110–112
 equal employment opportunity (EEO) laws, 423–424
 leaders and leadership, 373–376
 sexual harassment, 124–126
 General Agreement on Tariffs and Trade (GATT), 154, 156
General and Industrial Management (Payol), 7
 General environment, global, 148–154
 defined, 139
 demographic forces, 151–152
 economic forces, 149
 global forces, 154
 legal forces, 152–153
 political forces, 152–153
 sociocultural forces, 150–151
 technological forces, 149–150
 Generation of alternatives, decision-making process, 181–182
 Geographic structure, 254–255, 257–260
 Glass ceiling, 109–110

- Global environment, 136–169
 barriers to trade, 155–159
 cases for discussion, 167–169
 changing environment, 154–164
 competitive advantage, 28–30
 competitors, 146–148
 creativity, 193–194
 culture, national, 145, 160–164
 culture as a barrier, 156–157
 customers, 144–145
 demographic forces, 151–152
 distance as a barrier, 156–157
 distributors, 143–144
 diversity in workforce, 31–32
 e-commerce, 33
 economic forces, 149
 ethical standards, 30
 free trade, 154–159
 general environment, 139, 148–154
 global forces, 154
 Information Technology: global information system design, 145–146
 international expansion, 219–225
 IT utilization, 33
 legal forces, 152–153
 management process, overview, 27–33
 Management Snapshot: LG and competition, 137–138
 managerial hierarchy changes, 16–17
 national culture, 145, 160–164
 organizational environment, 138–139
 political forces, 152–153
 socially responsible standards, 30
 sociocultural forces, 150–151
 summary and exercises, 164–167
 task environment, 139, 140–142
 technological forces, 149–150
 trade barriers, 155–156
 Global forces, 139, 154
 Global geographic structure, 258
 Global Management
 American rice in Japan, 147–148
 Asians and Hispanic population growth, 112–113
 car manufacturing, 153
 diversity, 112–113
 e-commerce and customer responsiveness, 157–158
 human resources, 426–427
 Iglas' flexible factory, 500–501
 leaders and leadership, 363–364
 Levi Strauss, 222–223
 Nokia, Dow and LEGO performance, 259–260
 operations management, 500–501
 organizational control, 295–296
 organizational design, 259–260, 268–269
 outsourcing, 426–427
 Plexus self-managed work teams, 268–269
 Global Management—*Cont.*
 strategy formulation, 222–223, 228–229
 supply chain management, 142–143
 Toyota, 363–364
 Wal-Mart output control, 295–296
 world delivery business, 228–229
 Global organization, 27, 138
 Global outsourcing, 141
 Global product structure, 258
 Global strategy, 220
 Goal-setting theory of motivation, 335–337, 342
 Goals
 challenging, 212
 control process, 288–289
 defined, 5, 335
 difficulty and specificity of, 294, 335–337
 establish major, 211–212
 group dynamic
 accomplishment, 407
 groups and teams, 388
 management by objectives (MBO), 299
 organizational, 407
 planning managerial function, 8
 strategy formulation, 203–204, 209–212
 Gross profit margin, 292, 293
 Group cohesiveness, 405–408
 Group dynamics, 398, 399–400
 Group norms, 401
 Group roles, 399–400
 Grouping, organizational design, 248–264
 Groups and teams, 386–417
 cases for discussion, 415–417
 command groups, 395
 creativity, 192–193
 cross-functional teams, 262, 270–272, 391, 394, 401
 customer responsiveness, 389, 391
 decision making, 185–188
 defined, 388
 design of, 189, 260–262
 group dynamics, 398–408
 high performance management, 409–411
 Information Technology:
 Amazon pizza teams, 392–393
 Information Technology:
 expertise identification, synergies and ActiveNet, 390–391
 innovation, 389, 391–393
 interest groups, 398
 Management Snapshot:
 Southwest Airlines team culture, 387–388
 matrix structure, 260–262
 merit pay plan, 342–343, 344
 motivating, 409–410
 as motivators, 393
 organizational effectiveness, 388–393
 performance enhancement, 389–391
 Groups and teams—*Cont.*
 product team structure, 261, 262
 punishment, operant conditioning, 340
 R&D teams, 395
 self-managed work teams, 17, 18, 370, 395–396
 summary and exercises, 412–415
 task forces, 395
 team learning, 189
 top-management, 394
 types of, 394–398
 virtual, 396–397
 Groupthink, 187–188, 394
H
 Hawthorne effect, 46–47
 Herzberg's motivator-hygiene theory, 331
 Hierarchy
 of authority, 264–267
 of managers, 13–15, 16
 of needs, Maslow's, 329–331
 Hiring, diversity in, 123
 Hispanics
 business, 131–135
 in diverse workplace, 112–113
 as entrepreneurs, 121–122
 glass ceiling, 109–110
 Historical view of management theory, 41–48
 HIV-AIDS, 115–116, 424
 Hofstede's model of national culture, 161–163
 Honesty, trait model, 362
 Hostile work environment sexual harassment, 124
 HR; *see* Human resources (HR)
 Human managerial skills, 24, 25
 Human relations movement, 46–47
 Human resource management (HRM), 421–424
 Human resource planning, 425–426
 Human resources (HR), 420–453;
see also Employees and workers
 benefits, 441, 444
 cases for discussion, 451–453
 development, 434–436
 Diversity Focus: employee wellness benefits, 444–445
 Diversity Focus: mentoring, 434–435
 equal employment opportunity (EEO) laws, 423–424
 Ethics in Action: CEO compensation, 443
 external recruiting, 428–429
 Global Management:
 outsourcing, 426–427
 human resource management (HRM), 421–424
 human resource planning, 425–426
 internal recruiting, 429
 job analysis, 25, 427–428
 labor relations, 445–447
 Human resources (HR)—*Cont.*
 Management Snapshot: Semco, 419–420
 organizational design, 243, 247–248
 pay, 441–443
 performance appraisal, 436–439
 performance feedback, 436, 439–440
 planning, 425–426
 recruitment and selection, 424–429
 selection, 424–425, 429–432
 strategic human resource management, 421–424
 summary and exercises, 447–451
 training, 432–434, 435
 unions and labor relations, 445–447
 Human skills, 24
 Hungary, national culture, 163–164
 Hybrid structure, 262–263
 Hygiene needs, theory, 331
I
 Identity, group dynamics, 408
 Illumination, Hawthorne effect, 46–47
 Impersonal written communication, 467, 471–472
 Implementation, 181, 185, 233, 310
 Importing, 222
Inc., 69, 172
 Incentives, 409–410
 Income, 110–112, 116–117;
see also Pay
 Incomplete information, administrative decision-making model, 177
 India, 16–17
 Individualism, 161–162, 358
 Individuals
 creativity of, 190–191
 ethics of, 105, 106
 merit pay plan, 342–343, 344
 social loafing reduction, 410–411
 Ineffective communication, dangers of, 466–467
 Inequity, 333–335
 Inert culture, 305–307
 Informal appraisal, 440–441
 Informal groups, 394, 398
 Informal organization, Hawthorne effect, 47
 Information and the manager's job, 457–462; *see also* Communication
 communication media, 467–472
 completeness, 459
 control, 461–462
 coordination, 462
 costs, administrative decision-making model, 178–179
 decision making, 181–185, 461
 defined, 457
 distortion of, 477
 information systems, 459–460

- Information and the manager's job—*Cont.*
 information technology revolution, 473–476
 quality, 458
 relevance, 459
 richness of, 467–468, 480–481
 timeliness, 458
 useful information attributes, 457–459
- Information distortion, 477
- Information management system (MIS), 459
- Information overload, 472
- Information systems
 defined, 459
 limitation, 480–481
 management, 476–480
 technology, 459–460
- Information technology (IT)
 Amazon pizza teams, 392–393
 artificial intelligence (AI), 475, 480
 blogging, 485–486
 collaboration software and teams, 464
 communication, 460, 464, 472
 control systems, 287
 CRM at Empire Insurance, 18
 decision support systems, 478–479
 defined, 459
 e-stores, 460
 expectancy at Best Buy, 326
 expert systems, 480
 expertise identification, synergies and ActiveNet, 390–391
 global information system design, 145–146
 global utilization, 33
 IBM reinvention, 56–58
 Intel's 10 Commandments of Email, 472
 knowledge management, 247
 management process, overview, 18
 managerial hierarchy changes, 16–17
 managerial roles, 19–22
 motivation, 326
 operations information systems, 478
 organizational control, 287–288
 organizational design, 247, 272–275
 personal characteristics of managers, 56–58
 restructuring, 16–17
 revolution in, 473–476
 socioeconomic background, 116–117
 system limitation, 480–481
 teams, 390–391, 392–393
 traditional information hierarchy, 476–477
 transaction processing systems, 477–478
 utilization, and competitive advantage, 33
 virtual teams, 396–397
- Informational managerial roles, 20, 21, 120
- Initiating structure, behavior model, 363–364
- Innovation
 competitive advantage, 28, 29, 285, 286–287
 control process, 288
 decision making, 188
 defined, 189
 good communication, 463
 groups and teams, 389, 391–393
- Input
 control systems for, 287–288
 defined, 324
 equity theory, 332, 333–335
 expectancy theory, 324–325
 stage for, production system, 491, 495–496
- Instrumental value, 60, 61–62, 73
- Instrumentality, expectancy theory, 325, 327, 328
- Intangible rewards, 359–360
- Integrating mechanisms, organizational design, 269–272
- Integration
 rites of, 76–77
 role integration, 270, 271, 272
 vertical, 225–226
- Integrity, trait model, 362
- Intellectual stimulation, 372
- Intelligence
 emotional, 68–70, 73, 376
 trait model, 362
- Intensity of work, teams, 388
- Interest groups, 398
- Internal environment, 20
- Internal locus of control, 58
- Internal recruiting, human resources, 429
- International expansion
 franchising, 223–224
 functional-level strategy, 219–225
 global and multidomestic strategies, 220–221
 importing and exporting, 222
 licensing, 223
 strategic alliances, 224
 ways to expand, 222–225
 wholly owned foreign subsidiaries, 224–225
- Internet; *see also* Information technology (IT)
 blogging, 485–486
 computer networks, 474–475
 defined, 474
 international expansion, 219–225
- Interpersonal managerial roles, 20, 21–23, 120
- Interviews, human resource selection, 430
- Intrapreneurs, 313
- Intraversion, 53–54
- Intrinsically motivated behavior, 323
- Intuition, 174–176
- Inventory, 292, 293, 501–502
- Investors and stockholders, 94–95
- IT; *see* Information technology (IT)
-  Japan
 American rice in, 147–148
 collectivism, 161–162
 competition, 147
 distribution system, 143–144
 flexible manufacturing layout, 496, 499–500
keiretsu changes, 508–510
 leadership styles, 358
 self-reinforcement, 341
 sociocultural forces, 151
 Wal-Mart everyday low prices, 510–512
- JIT (just-in-time) inventory, 501–502
- Job analysis, 425, 427–428
- Job characteristic model, 250–251
- Job description, 427
- Job design, 248–251
- Job enlargement, 249
- Job enrichment, 249–250
- Job satisfaction, 63–65, 73
- Job simplification, 249
- Job specifications, 427
- Jobs, organizational design, 248–264; *see also* Employees and workers
 design of, 248–251
 divisional structure, 254–260
 enlargement, 249
 enrichment, 249–250
 functional structure, 252–253
 geographic structure, 254–255, 257–260
 grouping of, 251–264
 hybrid structure, 262–263
 job characteristic model, 250–251
 market structure, 254–255, 260
 matrix structure, 260–262
 organizational design, 251–264
 product structure, 254–257
 product team design, 261, 262
- Joint ventures, international expansion, 222, 224
- Judgment, reasoned, 174
- Just-in-time (JIT) inventory, 501–502
- Justice decision-making rules, 100, 101
- K**
- Kanban* system, 500–502
- Keiretsu*, 508–510
- Knowledge, trait model, 362
- Knowledge management, 247
- Knowledge management system, 275
- Korea, 141–142
-  LAN (local area network), 474
- Language, organizational culture, 77–78
- Large groups, 399
- Lateral moves, internal recruiting, 429
- Latinos; *see* Hispanics
- Law; *see* Legal issues
- Layout of facilities, 496–500
- Leader managerial role, 20, 21, 22, 120
- Leader-member relations, Fiedler's contingency model, 366, 367
- Leader style, Fiedler's contingency model, 365–367
- Leaders and leadership, 354–384
 behavior model, 363–364
 cases for discussion, 381–384
 charismatic, 372
 contingency models, 365–370
 defined, 357
 direct supervision, behavior control, 298–299
 Diversity Focus: Tower Automotive and Ligocki, 375–376
 emotional intelligence, 376
 gender, 373–376
 Global Management: Toyota, 363–364
 group dynamics, 400
 information for, 461
 Management Insight: Stamford Symphony Orchestra creativity, 368–369
 Management Snapshot: Whole Foods and Mackey, 355–356
 vs. managers, 358
 nature of, 357–362
 personal leadership style, 357–358
 style, 365–367, 374
 summary and exercises, 377–381
 trait model, 362–363
 transactional leadership, 373
 transformational leadership, 371–373
- Leaders substitutes contingency model, 369–370
- Leadership substitute, 369
- Leading, 8, 12, 15, 79
- Lean Six Sigma, 281
- Learning, 338
- Learning organization, 188–190, 308
- Learning theories of motivation, 338–341
 defined, 338
 operant conditioning theory, 338–340
 pay, 342
 social learning theory, 340–341
- Legal issues
 decision making, 182
 ethics, 91–92
 political and legal forces, 139, 152–153

- Legal issues—*Cont.*
 sexual harassment policy, 124–126
 societal ethics, 105
 Legitimate power, 359
 Letters and written
 communication, 467, 470–472
 Levels
 of managers, 13–15, 16, 299
 of planning, 203–206
 of strategy formulation, 213, 217–232
 Leverage ratio, 292, 293
 Liabilities, financial performance
 measure, 292–293
 Liaison roles, as integrating
 mechanism, 20, 21, 22, 120, 270, 271
 Licensing, international expansion,
 222, 223
 Limitations of information
 technology, 480–481
 Line manager, 264
 Liquidity ratio, 292, 293
 Loafing, social, 410–411
 Local area network (LAN), 474
 Locus of control, 58–59
 Long-distance learning, 435
 Long-term orientation, national
 culture, 163
 Long-term plans, 206
 Low-cost (business-level) strategy,
 9, 227, 229–231, 232
 Loyalty, brand, 147
- M**
- Mainframe, computer networks,
 474, 475
 Management
 defined, 5
 direct supervision, behavior
 control, 298–299
 diversity, 31, 90, 119–123
 information systems, 476–480
 nature of decision making,
 172–179
 scientific management, Taylor's,
 41–43
 self-managed work teams, 17,
 18, 370
 360-degree performance
 appraisal, 439
 Management by objectives
 (MBO), 299–300
 Management by wandering
 around, 468
 Management information system
 (MIS), 459
 Management Insight
 Citibank CRM, 493–494
 Gateway customer satisfaction,
 301–302
 GlaxoSmithKline product
 structure, 257
 leaders and leadership, 368–369
 Maden Technologies
 entrepreneurship, 312
 Mattel challenges, 210–211
 operations management,
 493–494, 501–502
- Management Insight—*Cont.*
 organizational control,
 301–302, 312
 organizational design, 257
 Stamford Symphony Orchestra
 creativity, 368–369
 strategy formulation,
 210–211
 United Electric *kanban* system,
 501–502
 Management process, overview,
 2–40
 cases for discussion, 37–40
 Diversity Focus: Union Bank of
 California competitive
 advantage, 31–32
 Ethics in Action: FDA and diet
 supplements, 30–31
 global challenges, 27–33
 Information Technology:
 CRM at Empire
 Insurance, 18
 management, defined, 5
 Management Snapshot: Home
 Depot and Lowe's
 performance
 management, 3–4
 Manager as Person: female
 CEOs Jung and Russo,
 10–11
 Manager as Person: Job's
 transformation of Apple,
 25–27
 manager realities, 23
 managerial functions, 7–13
 managerial role, 19–23
 managerial skills, 13–17, 23–25
 performance achievement, 5–6
 reasons to study, 6–7
 summary and exercises, 33–37
 types of managers, 13–19
 Management Snapshot
 ABS decisions, 171–172
 code of ethics strengthening,
 89–90
 communication, 455–456
 decision making, 171–172
 global environment, 137–138
 Herman Miller, 455–456
 Home Depot and Lowe's high
 performance
 management, 3–4
 human resources, 419–420
 leaders and leadership, 355–356
 LG and competition, 137–138
 L.L.Bean, 201–202
 Lucent reorganization, 241–242
 management process,
 overview, 3–4
 motivation, 321–322
 operations management,
 489–490
 Oracle, 283–284
 organizational control, 283–284
 organizational design, 241–242
 PAETEC employees, 51–52
 personal characteristics of
 managers, 51–52
 SAS employee motivation,
 321–322
 Semco, 419–420
 Southwest Airlines' team
 culture, 387–388
- Management Snapshot—*Cont.*
 strategy formulation, 201–202
 teams, 387–388
 Toyota, 489–490
 Whole Foods leadership,
 355–356
 Management theory, historical
 view of, 41–48
 Manager as Person
 Apple, Job's transformation
 of, 25–27
 business creation and
 determination, 121–122
 Campbell Soup Co., Conant at,
 214–216
 communication, 479–480
 decision making, 175–176
 diversity, 121–122
 female CEOs Jung and Russo,
 10–11
 Gateway and eMachines,
 Inouye at, 244–245
 Hopkirk facilities layout
 improvement, 498, 499
 INC. and Goldhirsh, 69
 management process, overview,
 10–11, 25–27
 Merck, Lewent at, 479–480
 operations management,
 498, 499
 organizational control,
 304–305
 organizational design,
 244–245
 overconfidence, 175–176
 personal characteristics of
 managers, 69
 strategy formulation, 214–216
 UPS, Casey at, 304–305
 Managerial action, 78–80
 Managerial functions, 7–13
 controlling, 8, 12–13, 15
 defined, 13
 leading, 8, 12, 15
 organizing, 8, 11–12, 15
 overview, 7–8
 planning, 8–10, 15, 30
 Managerial roles, 19–23
 changes in, 16–19
 decisional, 20–21
 defined, 19
 diversity, 119–121
 informational, 20, 21
 interpersonal, 20, 21–23
 Mintzberg's, 19–23
 Managers; *see also* Information and
 the manager's job
 areas of responsibility, 15–16
 daily realities, 23
 as ethical stakeholders, 94,
 95–96
 ethics, 95–96, 102–104
 and free trade, 159–160
 hierarchy of, 13–15, 16
 vs. leaders, 358
 levels of, 13–15, 16
 organizational commitment, 63,
 65–66
 personal leadership style,
 357–358
 planning by, 206
 self-awareness, 58
 types of, 13–19
- Managers, personal characteristics
 of, 50–87
 attitudes, 62–66
 cases for discussion, 83–87
 Diversity Focus: balanced life
 and organizational
 commitment, 63
 emotional intelligence, 68–70
 emotions, 67–68
 Ethics in Action: honesty, 62
 Ethics in Action: whistleblowers,
 58–59, 62
 Information Technology: IBM
 reinvention, 56–58
 Management Snapshot:
 PAETEC employees,
 51–52
 Manager as Person: Goldhirsh
 and INC., 69
 mood, 67–68
 organizational culture, 71–80
 personality, 52–60
 summary and exercises,
 80–83
 values, 60–62
 Manufacturing, layout flexibility,
 496, 498–501
 Marijuana, ethics of, 92–93
 Market structure, 254–255, 260
 Maslow's hierarchy of needs,
 329–331
 Mass market, 167–168
 Mass-production technology,
 246–247
 Master of Business Administration
 (MBA), 6, 23–24
 Matrix structure, 260–262,
 270, 272
 Maturity, trait model, 362
 MBA (Master of Business
 Administration),
 6, 23–24
 MBO (management by
 objectives), 299–300
 McClelland's need for
 achievement, affiliation
 and power, 59–60,
 331–332
 Meaning and purpose, job
 characteristics model,
 250, 251
 Measurement; *see also*
 Organizational control
 performance, 288–290,
 292–293
 Media for communication,
 467–472
 Mediator, collective
 bargaining, 447
 Medium, communication
 process, 465
 Memos and written
 communication, 467,
 470–472
 Mental models, complex, 189
 Mentor, 434
 Merit pay plan, 342–343, 344
 Message, 464–465
 Mexico, NAFTA, 154, 159–160
 Middle managers
 defined, 14
 delegation from top
 manager, 185

- Middle managers—*Cont.*
 minimum chain of command, 267
 performance, 13, 14, 15–17
 Minimum chain of command, 267
 Minnesota Satisfaction Questionnaire, 64
 Mintzberg's managerial roles, 19–23
 MIS (management information system), 459
 Mission, in strategy formulation, 209–212
 Mission statement, 203
 Models for decision-making process, 179–180
 Monitor managerial role, 20, 22, 120
 Mood, 60, 67–68, 73
 Mood questionnaire, 68
 Moral rights decision-making rules, 100–101
 Mores, 161
 Motivation, 320–353
 cases for discussion, 349–353
 defined, 322
 Diversity Focus: Nike diverse customer appeal, 328–329
 Diversity Focus: Time Warner turnaround, 336–337
 equation for, 324
 equity theories, 332–335
 expectancy theory, 324–329
 goal-setting theory, 335–337
 of groups and teams, 409–410
 Information Technology: expectancy at Best Buy, 326
 job characteristics model, 250–251
 learning theories, 338–341
 Management Snapshot: SAS employee motivation, 321–322
 nature of, 322–324
 need theories, 329–332
 pay, 342–345
 summary and exercises, 345–349
 Motivator-hygiene theory, Herzberg's, 331
 Motivator needs, theory, 331
 Motivators, groups and teams as, 393
 Multidomestic strategies, 220–221
- N**
- Nation, ethics in, 97–99
 National culture, 145, 150, 160–164
 National Labor Relations Act (1935), 446
 National Labor Relations Board (NLRB), 446
 Native Hawaiians, in diverse workplace, 112
 Nature of managerial decision making, 172–179
 Need, defined, 329
 Need for achievement, affiliation and power, McClelland's, 331–332
 Need theories of motivation, 329–332
 defined, 329
 Herzberg's motivator-hygiene theory, 331
 Maslow's hierarchy of needs, 329–331
 McClelland's need for achievement, affiliation and power, 331–332
 pay, 342
 Needs assessment, 308–309, 432
 Negative affectivity as personality trait, 55
 Negative mood, 67–68
 Negative reinforcement, operant conditioning, 338–339, 340
 Negotiator managerial role, 20, 22, 120
 Network structure, 273
 Networking, computer, 474–475
 Networks, TV, diversity on, 113–114
 New business development, 218–219
 NLRB (National Labor Relations Board), 446
 Noise, communication process, 465
 Nominal group technique, 192–193
 Nonprogrammed decision making, 174–176, 179–180, 478
 Nonroutine technology, 246, 290
 Nonverbal communication, 465–466
 Norming, self-managed work teams, 401
 Norms
 in bureaucratic theory, Weber's, 44
 defined, 60, 160
 group dynamics, 401–407
 national culture, 160–161
 organizational culture, 73, 74–76, 79–80
 North American Free Trade Agreement on Tariffs and Trade (NAFTA), 154, 159–160
 Not-for-profit organizations, 27, 149
 “Now Who’s Boss” day, 525–526
 Nurturing orientation, national culture, 163
- O**
- Objective appraisal, 437–438
 Observational learning (vicarious learning), 340–341
 OCBs (organizational citizenship behaviors), 64
 Occupational Safety and Health Act (1970), 423, 445
 On-the-job training, 432, 433–434
 Openness to experience, 54, 56
 Operant conditioning theory, 338–340
 Operating budgets, 295
 Operating system software, 475
 Operations information systems, 478
 Operations management, 488–512
 cases for discussion, 508–512
 competitive advantage, 490–491
 customer responsiveness improvement, 491–494
 defined, 490
 efficiency improvements, 495–504
 Ethics in Action: human cost of productivity improvements, 504–505
 facilities layout, 496–500
 flexible manufacturing layout, 496, 498–501
 Global Management: Igus’ flexible factory, 500–501
 just-in-time inventory, 501–502
 Management Insight: Citibank CRM, 493–494
 Management Insight: United Electric *kanban* system, 501–502
 Management Snapshot: Toyota, 489–490
 Manager as Person: Hopkirk facilities layout improvement, 498, 499
 process reengineering, 502–503
 quality improvement, 494–495
 self-managed work teams, 502
 summary and exercises, 505–508
 Operations manager, 490, 491
 Opportunities
 decision making, 172–173
 distributors, 143–144
 economic forces, 149
 organizational environment, 138
 SWOT analysis, 138, 213–214
 vertical integration, 225
 Optimum decision, 176–177
Oregon Business, 172
 Organizational architecture, 242
 Organizational behavior, Hawthorne effect, 47
 Organizational change, 307–311
 assessment of need, 308–309
 decision-making regarding, 309–310
 defined, 307–308
 evaluation, 310–311
 implementation, 310
 obstacles to, 310
 organizational control, 307–311
 process of, 308, 309
 Organizational citizenship behaviors (OCBs), 64
 Organizational commitment, 63, 65–66
 Organizational commitment questionnaire, 66
 Organizational control, 282–319
 behavior control, 298–303
 cases for discussion, 317–319
 clan control, 303–307
 control process, 288–292
 control systems, 287–288
 defined, 285
 entrepreneurship, 311–313
 Global Management: Wal-Mart output control, 295–296
 importance of, 285–287
 information technology (IT), 287–288
 Management Insight: Gateway customer satisfaction, 301–302
 Management Insight: Maden Technologies entrepreneurship, 312
 Management Snapshot: Oracle, 283–284
 Manager as Person: Casey at UPS, 304–305
 measurement system designs, 291
 organizational change, 307–311
 output control, 291–298
 process of, 288–291
 purpose if, 284–285
 summary and exercises, 314–317
 Organizational culture, 71–80
 adaptive vs. inert, 305–307
 ASA framework, 71–72, 74
 ceremonies, 76–78
 defined, 71, 303
 ethics, 104–109
 founder values, 74
 learning organization, 188–190
 managerial action, 78–80
 norms, 74–76
 as organizational control system, 291
 personal characteristics of managers, 71–80
 rites, 76–78
 socialization, 74–76
 values, 73–74
 Organizational design, 240–281
 B2B network structures, 272–275
 cases for discussion, 279–281
 coordinating functions and divisions, 264–272
 defined, 240–241, 243
 Ethics in Action: sweatshops and shoe manufacturing, 274–275
 geographic structure, 254–255, 257–260
 Global Management: Nokia, Dow and LEGO performance, 259–260
 Global Management: Plexus self-managed work teams, 268–269
 hierarchical structure, 266–267, 476–477
 human resources, 247–248
 hybrid structure, 262–263
 information technology (IT), 247, 272–275
 job design, 248–251
 job grouping, 251–264

- Organizational design—*Cont.*
 Management Insight:
 GlaxoSmithKline
 product structure, 257
 Management Snapshot: Lucent
 reorganization, 241–242
 Manager as Person: Inouye at
 Gateway and
 eMachines, 244–245
 market structure, 254–255, 260
 matrix structure, 260–262
 organizational environment,
 243–244
 organizational structure,
 11–12, 243
 product structure, 255–257
 product team structure,
 261, 262
 strategic alliances, 272–275
 strategy, 244
 summary and exercises,
 275–279
 tasks, grouping of, 248–251
 technology, 245–247
 Organizational effectiveness,
 groups and teams,
 388–393
 Organizational environment,
 138–139, 243–244
 Organizational goals,
 293–294, 407
 Organizational learning,
 188–190, 308
 Organizational performance, 5
 Organizational resources,
 20, 21–22, 120
 Organizational socialization,
 75–76
 Organizational structure; *see also*
 Organizational design
 defined, 11–12, 243
 hierarchy, 266–267, 476–477
 Organizations; *see also specific*
companies [in company
 index]
 defined, 5
 global organizations, 138
 merit pay plan, 342–343, 344
 not-for-profit, 27, 149
 planning importance, 207–208
 profit-oriented, 16–17, 149
 service organizations, 301
 Organizing
 defined, 11, 243
 information for, 461
 as managerial function,
 8, 11–12, 15
 Outcome
 defined, 323
 expectancy theory, 325, 327
 Herzberg's motivator-hygiene
 theory, 331
 job characteristics model,
 250, 251
 motivation equation, 324
 need theories, 329
 operant conditioning,
 338–340
 Output, 289–298
 behavior control, 289–290
 bureaucratic control, 303
 controls for, 289–298, 303
 equity theory, 332, 333–335
 Output—*Cont.*
 financial performance metrics,
 292–293
 operating budgets, 295
 organizational change, 307
 organizational control,
 291–298
 organizational culture, 303
 organizational goals, 293–294
 performance measures,
 292–293
 problems with, 296–298
 stage of, production system, 491,
 492, 495–496
 systems for, 287–288
 Outsource and outsourcing
 defined, 16, 274, 425
 global, 16–17, 141–142
 human resource planning,
 425–427
 Overpayment inequity, 333–334
- P**
- Pacific Islander, in diverse
 workplace, 112
 Paper-and-pencil selection tests,
 430, 431
 Paper trail, communication
 media, 468
 Partial productivity, 496
 Participation levels, group
 dynamics, 406
 Participative behavior, 368,
 374–375
 Passage, rites of, 76
 Path-goal theory, House's
 contingency model,
 367–369, 370
 Pay, 441–443
 executive compensation, 96
 human resource management
 (HRM), 423
 human resources, 441–443
 income, 110–112, 116–117
 level of, 441–442
 merit pay plan, 342–343, 344
 motivation, 342–345
 salaries, 342–345
 structure of, 442–443
 Peer-appraisals, performance,
 438–439
 Perception, equity theory, 332
 Performance; *see also*
 Organizational control
 achievement of managerial
 goals, 5–6
 appraisal of, 421, 422, 423,
 436–439
 bureaucratic control, 303
 coercive power, 360
 control process, 288–290
 controlling managerial
 functions, 8, 12–13
 decentralization of
 authority, 268
 efficiency and effectiveness, 6
 enhancement of, 389–391
 ethical behavior, 30, 102–104
 expectancy theory, 325, 327
 feedback, 421, 422, 436,
 439–440
 Performance—*Cont.*
 by groups and teams, 389–391,
 409–411
 high performance group
 management, 409–411
 measurement, 288–290,
 292–293
 merit pay plan, 342–343, 344
 monitor managerial role, 20, 21
 motivation equation, 324
 organizational, defined, 5
 organizational change, 307–308
 output control measures,
 292–293
 scientific management, Taylor's,
 41–43
 on selection tests, 430, 431
 self-managed work teams, 401
 socially responsible
 standards, 30
 top managers, 13, 14–17
 Performance appraisal, 421, 422,
 423, 436–439
 Performance feedback, 421, 422,
 436, 439–440
 Performance measures, output
 control, 292–293
 Performance selection tests,
 430, 431
 Persistence, and motivation,
 322
 Personal characteristics of
 managers; *see* Managers,
 personal characteristics of
 Personal leadership style,
 357–358
 Personality selection tests,
 430, 431
 Personality traits, 52–60
 agreeableness, 55–56
 Big Five personality traits,
 52–58
 conscientiousness, 56
 defined, 52
 extraversion, 53–54, 67
 locus of control, 58–59
 need for achievement, affiliation
 and power, 59–60
 negative affectivity, 55
 openness to experience, 56
 organizational culture, 73
 self-esteem, 59
 Personally addressed written
 communication, 467,
 470–471
 Phone-like communication,
 469–470
 Physical ability selection tests,
 430, 431
 Physiological needs, Maslow's,
 329, 330
 Piece-rate pay, 344–345
 Planning, 202–209
 defined, 8, 202
 human resources, 425–426
 importance of, 207–208
 information for, 461
 levels of, 203–206
 as managerial function,
 8–10, 15
 by managers, 206
 organizational culture, 78–79
 scenario planning, 208–209
 Planning—*Cont.*
 standing and single-use
 plans, 207
 steps in, 202–203
 strategy formulation, 202–209,
 213, 233
 strategy implementation,
 204, 233
 time horizon, 206
 Policy, 207
 Political and legal forces, general
 global environment, 139,
 152–153
 Porter's five forces model, 216,
 229–230
 Portfolio strategy, 219
Portland Business Journal, 172
 Position power, Fiedler's
 contingency model,
 366, 367
 Positive mood, 67–68
 Positive reinforcement, operant
 conditioning, 338
 Potential competitors, 146
 Poverty, 116–117
 Power
 coercive, 360
 distance of, national culture,
 162–163
 empowerment, 361–362
 expert, 360–361
 and leadership, 358–361
 legitimate, 359
 needs for, McClelland's, 59–60,
 331–332
 position power, Fiedler's
 contingency model, 366
 referent, 361
 reward, 359–360
 Practical decision-making rules,
 100, 101–102
 Practicality, decision making, 182
 Pregnancy Discrimination Act
 (1978), 111, 424
 Premium price, differentiation,
 227–228, 231–232
 Prescriptive classical decision-
 making model, 176–177
 Price
 customer satisfaction, 492
 differentiation, 227–228
 perceived value, 231–233
 quality improvement, 494–495
 Privatization, 152
 Proactivity, decision making, 181
 Process layout, 497
 Process reengineering, 502–503
 Product structure, 254–256, 258
 Product team structure, 261, 262
 Production blocking, 192
 Production system, 490–493
 Productivity, efficiency
 improvements, 495–504
 Products
 customer satisfaction, 492
 facilities layout, 496–497
 five forces model, 216
 flexible manufacturing layout,
 496, 498–501
 organizational design, 254–256
 team design, 261, 262
 Professional ethics, 105–106
 Profit operating budgets, 295

- Profit-oriented organizations, 16–17, 149; *see also specific companies* [in company index]
- Profit ratio, 292, 293
- Profit sharing, 345
- Programmed decision making, 173–174
- Programs, 207
- Projects, 207
- Promotions, internal recruiting, 429
- Protege, 434
- Psychological states, job characteristics model, 250–251; *see also* Motivation
- Punishment, operant conditioning, 339–340
- Q**
- Quality
 - competitive advantage, 28, 29, 285, 286
 - control process, 288
 - customer satisfaction, 492
 - customers, responsiveness to, 490
 - defined, in operations management, 490
 - improvements and price, 494–495
 - of information, 458
 - operations management, 494–495
 - organizational culture, 77–78
 - total quality management (TQM), 29
- Quick ratio, 292, 293
- Quid pro quo sexual harassment, 124
- R**
- Race and diversity, 112–114, 423–424
- R&D (research & development), 227, 232, 395, 399
- Real time information, 458
- Reasoned judgment, 174
- Reasons to study management process, 6–7
- Receiver, communication process, 465
- Recognition, decision-making process, 180–181
- Recruitment of human resources, 429–432
 - background information, 429–430
 - defined, 424–425
 - human resource management (HRM), 421, 422, 423
 - interviews, 430
 - process of, 429–432
 - references, 431–432
 - reliability and validity, 432
 - system for, 424–425
 - testing, 431
 - tools summary, 430
- Reengineering, process, 502–503
- References, human resources recruitment, 430, 431–432
- Referent, equity theory, 332
- Referent power, 361
- Regional structure, 257–258
- Regulations as entry barriers, 147
- Reinforcement, learning theory, 338–341
- Related diversification, 218
- Relationship-oriented leaders, 365–366
- Relevance of information, 459
- Reliability, human resources selection, 430, 432
- Religion, as diversity, 114, 423–424
- Reporting, matrix structure, 260–262
- Reputation, 103
- Research & development (R&D), 227, 232, 395, 399
- Resource allocator managerial role, 20, 21–22, 120
- Resources; *see also* Human resources (HR)
 - defined, 5
 - for groups, 401
 - organizational, 20, 21–22, 120
- Responsibility, job characteristics model, 250, 251
- Restructuring, 16–17
- Result performance appraisal, 437
- Retailer brand name, 230
- Return on investment (ROI), 292, 293
- Revenue operating budgets, 295
- Review, management by objectives (MBO), 299
- Revolution, in information technology, 473–476
- Reward power, 359–360
- Richness of information, 467–468, 480–481
- Risk, 178–179, 224
- Rites, in organizational culture, 76–78
- Rites of enhancement, 76, 77
- Rites of integration, 76–77
- Rites of passage, 76
- Rivalry, five forces model, 216
- ROI (return on investment), 292, 293
- Role integration, 270, 271, 272
- Role making, 400
- Role playing, 433
- Roles, group dynamics, 399–400
- Rolling plans, 206
- Rules
 - bureaucratic control, 300, 302–303
 - in bureaucratic theory, Weber's, 44
 - defined, 207
 - ethical decision-making, 99–102
 - programmed decision making, 173–174
- S**
- Safety needs, Maslow's, 329, 330
- Salary, 342–345; *see also* Pay
- Sarbanes-Oxley Act, 90
- Satisfaction
 - customer, 209, 492
 - job, 63–65, 73
 - team employees, 393
- Satisficing, 179
- Scanlon plan, 344–345
- Scenario planning, 208–209
- Scientific management, Taylor's, 41–43
- Selection of human resources, 429–432
 - background information, 429–430
 - defined, 424–425
 - human resource management (HRM), 421, 422, 423
 - interviews, 430
 - process of, 429–432
 - references, 431–432
 - reliability and validity, 432
 - system for, 424–425
 - testing, 431
 - tools summary, 430
- Self-actualization needs, Maslow's, 329, 330
- Self-appraisals, performance, 438–439
- Self-confidence, trait model, 362
- Self-efficacy, learning theory, 340, 341
- Self-esteem, 59, 340
- Self-managed work teams
 - defined, 395
 - development, 400–401
 - management of, 17, 18, 370, 395–396
 - operations management, 502
 - organizational design, 268–269
 - role making, 400
- Self-reinforcement, learning theory, 340, 341
- Self-reinforcer, 341
- Sender, communication process, 464–465
- September 11, 2001, terrorist attacks, 116
- Servers, computer networks, 474, 475
- Service-based economy, 29
- Service organizations, 301
- Sexual harassment, 124–126
- Sexual orientation (gay/lesbian), 117–118
- Short-term orientation, national culture, 163
- Short-term plans, 206
- Simplicity of integrating mechanism, 270
- Simulations, for training, 433
- Single business concentration, corporate-level strategy, 217–218
- Single-use plans, 207
- Situational characteristics
 - Fiedler's contingency model, 366–367
 - leader substitutes model, 369–370
- Situational interview
 - questions, 430
- Six Sigma, 281, 421–422
- Size of group, 399, 405, 407
- Skills
 - in job characteristics model, 250
 - managerial, 13–17, 23–25
 - Slavery, ethics of, 92
- Small-batch technology, 246
- Small groups, 399
- Social learning theory, 340–341
- Social loafing, 410–411
- Social Security benefits, 444
- Social structure, 150
- Socialization, organizational culture, 74–76
- Socially responsible standards, 30
- Societal ethics, 104–105
- Societal issues, 6–7, 97–99, 104–105
- Sociocultural forces, global environment, 139, 150–151
- Socioeconomic background, 116–117
- SOPs (standard operating procedures), 44, 207, 300, 303
- Span of control, 264–265
- Specialization, strategies, 230–231
- Specificity of goals, 294, 335–337
- Speech recognition software, 476
- Speed, competitive advantage, 28, 29
- Spoken communication, 467, 469–470
- Spokesperson managerial role, 20, 22, 65, 120
- Staff manager, 264
- Stakeholders
 - defined, 94
 - ethical, 90, 94–108
- Standard operating procedures (SOPs), 44, 207, 300, 303
- Standards, 288–289, 300–301
- Standing plans, 207
- Stereotypes, 109, 374
- Stock options, 343–344
- Stockholders, 94–95
- Stories, organizational culture, 77
- Storming, self-managed teams, 400–401
- Strategic alliances, 222, 224, 272–275
- Strategic human resource management, 421–424
- Strategy, 9, 202
- Strategy formulation, 200–239
 - business-level strategy, 204, 226–231
 - cases for discussion, 237–239
 - competitive advantage, 232
 - corporate-level strategy, 204, 217–226
 - defined, 212
 - five forces model, 216
 - functional-level strategy, 205, 231–232
 - Global Management: Levi Strauss, 222–223
 - Global Management: world delivery business, 228–229
 - goal setting, 203–204, 209–212
 - implementation, 233
 - levels of, 213, 217–232

Strategy formulation—*Cont.*

- Management Insight: Mattel challenges, 210–211
- Management Snapshot:
 - L.L.Bean, 201–202
- Manager as Person: Campbell Soup Co. and Conant, 214–216
- mission determination, 202–203, 209–212
- organizational design, 243, 244
- planning, 202–209, 233
- summary and exercises, 233–237
- SWOT analysis, 213–214
- Strengths, SWOT analysis, 138, 213–214
- Stress, trait model, 362
- Stretch goals, 294
- Structured interviews, 430
- “Stuck in the middle” five forces model, 229–230
- Style of personal leadership, 357–358
- Subjective appraisal, 437–438
- Subordinate appraisals,
 - performance, 438–439
- Subordinates
 - behavior control, 298–299
 - characteristics of, 369–370
 - intellectual stimulation, 372
 - transformational leadership, 371–372
- Substitution, five forces model, 216
- Success, group dynamics, 408
- Supervisors (first-line managers), 13, 14, 15–17, 438
- Suppliers
 - defined, 140
 - as ethical stakeholders, 94, 97, 98
 - five forces model, 216
 - task environment, 139, 140–143
- Supply forecasting, 425
- Supportive behavior, path-goal theory, 368
- SWOT analysis, 138, 213–214
- Synchronous technologies, 397
- Synergy, 218, 389–390
- Systems thinking, 189

T

- Tall organizational hierarchy, 266–267
- Tangible rewards, 359–360
- Targets, control process, 288–289
- Tariff, 155, 159
- Task environment, 139, 140–146, 148
- Task force teams, 270, 271, 395
- Task-oriented leaders, 366
- Task structure, 366, 367
- Tasks
 - analyzability of, 246
 - job characteristics model, 250–251
 - organizational grouping of, 248–251
 - variety of, 246
- Teams; *see* Groups and teams
- Technical managerial skills, 24–25
- Technology
 - complexity, 246, 290
 - defined, 149, 245
 - forces of, general global environment, 139, 149–150
 - as nonroutine, 246, 290
 - organizational design, 243, 245–247
- Telecommuting, 470–471
- Telephone communication, 469–470
- Television, diversity on, 113–114
- Terminal value, 60–61, 73
- Testing, human resources
 - selection, 430, 431
- Theory X, McGregor's, 47–48
- Theory Y, McGregor's, 47–48
- Threat
 - decision making, 172–173
 - distributors, 143–144
 - economic forces, 149
 - organizational environment, 138
 - suppliers, 140, 141
 - in SWOT analysis, 138, 213–214
- 360-degree performance appraisal, 439
- Time horizon, 206
- Time issues
 - communication media, 468
 - constraints, administrative decision-making model, 178–179
 - goal setting, 212
 - group dynamic development, 400–401
 - information timeliness, 458
 - leadership styles and culture, 358
 - for planning, 206
 - punishment, operant conditioning, 340
 - time horizon for planning, 206
 - time spent on managerial functions, 15
- Times-covered ratio, 292, 293
- Title VII of the Civil Rights Act (1964), 111, 423, 424
- Top-down change, 310
- Top-management teams, 15, 394, 399, 442–443
- Top managers
 - centralization of authority, 267–268
 - CEOs and COOs, 14–15
 - control process, 289
 - corporate-level strategy, 219
 - decision-making, 185, 196
 - defined, 14
 - diversity, 111–112
 - ethical behavior, 95, 106
 - executive compensation, 96
 - five forces model, 229
 - gender, 111–112
 - group creativity, 192, 193
 - job grouping, 251
 - middle manager delegation, 185

Top managers—*Cont.*

- minimum chain of
 - command, 267
- organizational change, 310
- organizational culture, 73, 78–80
- organizational learning, 189
- performance, 13, 14–17
- planning, 78–79, 203–207, 246
- sexual harassment, 125
- sexual orientation, 117
- sociocultural forces, 150
- stock options, 343–344
- stockholder responsibility, 95
- Total factor productivity, 495–496
- Total quality management (TQM), 29
- TQM (total quality management), 29
- Trade barriers, 154, 155–159
- Traditional information hierarchy, 476–477
- Training, human resources, 421–423, 432–434, 435
- Trait model, leadership, 362–363
- Trait performance appraisal, 436–437
- Transaction-processing systems, 477–478
- Transactional leadership, 373
- Transformational leadership, 371–373
- Transmission phase,
 - communication, 464–465
- Trust, 102
- Turnover, diversity in, 123
- TV, diversity on, 113–114
- Two-boss employees, 260–261

U

- Uncertainty, 163, 178–179
- Uncertainty avoidance, 163
- Underpayment inequity, 333–334
- Unemployment benefits, 444
- Unethical behavior, 102–104
- Unions and labor relations, 445–447
- Units, command group, 395
- Unity in effective plans, 208
- Unrelated diversification, 218–219
- Unstructured interviews, 430
- Useful information, attributes of, 457–459
- Utilitarian decision-making rules, 99–100

V

- Valence, expectancy theory, 325, 327, 328
- Validity in selection, human resources, 430, 432

Value added, functional-level strategy, 231–232

Values

- defined, 160
- of founder, 74
- functional-level strategies, 231–232
- of managers, 60–62
- national culture, 160–161
- organizational culture, 73–74, 79–80
- systems of, 60
- Variety in managerial life, 23
- Verbal communication, 465–466, 467, 469–470
- Vertical integration, 225–226
- Vicarious learning, 340–341
- Video cases, 519–534; *see also* Cases for discussion
 - British Petroleum (BP), 526–527
 - Cirque du Soleil, 522–523
 - Container Store, 527–528
 - eBay, 533–534
 - Enron, 521–522
 - evolution of management, 520
 - GE and Welch's legacy, 528–529
 - Hillerich & Bradsby (H&B), 531–532
 - JetBlue Airways, 524–525
 - Louisville Slugger, 531–532
 - McFarlane Companies, 520–521
 - NASA and *Columbia* disaster, 523–524
 - “Now Who's Boss” day, 525–526
 - Patagonia, 530–531
 - Pike Place Fish, 529–530
 - Starbucks, 532–533
 - Wild Oats, 519
- Videoconferences, 469
- Videos, for training, 433
- Virtual teams, 396–397
- Vision, 8–10, 12, 189
- Voice mail, 470

W

- Wages, 441–442; *see also* Pay
- Weaknesses in SWOT, 138, 213–214
- Whites, in diverse workplace, 112
- Wholly owned foreign subsidiaries, 222, 224–225
- Wireless communication, 473–474
- Women in workplace; *see* Gender
- Workers; *see* Employees and workers
- Workers' compensation, 444
- World Trade Organization (WTO), 156
- Written communication, 467, 470–472

Companies

A

A. T. Kearney Inc., 511
 ABB Group, 86–87
 ABC, 143
 Accenture, 6, 144
 ActiveNet, 390–391
 Adidas, 273–274
 Advantica, 123
 Advertising.com Inc., 486, 487
 Aeon Co., 511
 AES Corporation, 396
 Aetna Life & Casualty, 123
 Agricultural Data Systems, 344
 AIG (American International Group), 129–131
 Airborne Express, 228–229, 461–462, 478
 Airbus Industries, 17
 Albertsons Inc., 383–384
 Alcoa Inc., 39, 381
 Alliance Funding, 439
 Allied Signal Inc., 439
 Amazon.com, 56, 144, 146, 147, 157, 158, 202, 221, 392–393, 459
 AMD, 140, 217
 America Online (AOL), 140, 176, 239, 336–337, 486–487
 American Airlines, 123
 American Greetings Corp., 469, 471
 American International Group (AIG), 129–131
 American Museum of Natural History, 130
 American Psychological Association, 64
 American Stores Co., 383
 Ameritrade, 146
 Amstrad, 220
 Anderson School of Management, University of California - Los Angeles, 118
 Angiotech Pharmaceuticals, 191
 Anthem, 319
 AOL (America Online), 140, 176, 239, 336–337, 486–487
 AOL-Time Warner, 176, 336–337
 Apollo, 180, 182
 Apple Computer, 7, 8, 25–27, 72, 137, 178, 239
 Arcelor, 168
 Armani, 220, 230
 Arthur Andersen, 89, 93, 225, 275
 ASDA, 190
 Astra Pharmaceuticals, 479
 Astra Zeneca International, 444
 AT&T Corp., 9, 17, 212, 431, 439, 442
 Audi, 238
 Austin Chemical, 67
 AutoPacific Inc., 238
 Autopolis, 238

Avis, 224
 Avon Products, 10, 70, 111, 158, 374

B

Babson College, 435
 Bank of America Corp. (BoFA), 451–452
 Barnes & Noble, 159
 Baxter International Inc., 439
 BBC, 159
 Bendixen & Associates, 134
 Benxi Iron & Steel (Group) Co., 169
 Berkshire Hathaway, 129
 Best Buy, 244, 326
 BET, 256
 Beth Israel Deaconess Hospital, 186–187
 BIC, 227, 229
 Bigg's, 84
 Black & Decker, 262
 Black Like Me, 366
 BlackBerry, 198–199
 Bladelogic, 427
 Blockbuster, 256
 Blu-Ray, 239
 Bluelight.com, 459, 460
 BMG, 239
 BMW, 230, 369
 Bob Evans Farms Inc., 471
 The Body Shop, 56
 Boeing, 141, 221, 350–353, 388, 427, 462, 481, 493
 BoFA (Bank of America Corp.), 451–452
 The Bombay Company, 222
 Bonaminio, Jim, 83–85
 Bosch, 509, 510
 Boston Short-Term Rentals, 21–23
 BP Amoco, 224
 BP (British Petroleum), 526–527
 British Petroleum (BP), 526–527
 Brooks Brothers, 257
 Buck\$ Dollar Stores, 84

C

C. R. England Refrigerated Trucking Company, 386
 CAIB (*Columbia Accident Investigation Board*), 183
 California Institute of Technology, 395
 Calvert Group, 122–123
 Calvin Klein, 222
 Campbell Soup Co., 213–216
 Canon, 428
 Cap Gemini, 144
 CareGroup, 186

Carrefour, 511
 Catalyst, 110–111
 Cato Institute, 427
 CBS, 143, 256
 Center for Media and Public Affairs, 113
 Challenger, Gray and Christmas, 95
 Channel, 220, 230
 Charles Schwab, 146
 Chevron Corporation, 124
 Children Now, 113
 Children's Choice Learning Center, 116
 Chrysler, 123, 153, 176, 286, 425, 431
 Ciba-Geigy, 382
 Circuit City, 326
 Cirque du Soleil, 522–523
 Cisco Systems, 140, 208, 211–212, 427, 428
 Citibank, 491, 493–494, 502
 Citizens Financial Group Inc., 365–366
 CNN, 159
 Coca-Cola, 123, 141, 144, 151, 154, 224, 226, 227, 230, 232, 428, 443
 Coldbath Fields Prison, 93
 Collaboration Software, 463
 Columbia Accident Investigation Board (CAIB), 183
 Compaq Computer, 8, 149, 313, 397, 496
 Container Store, 349–350, 527–528
 Coram Healthcare Corporation, 362
 Costco, 159, 226
 Cott Corporation, 230
 Cross, 227, 229
 C.V. Starr & Co., 130
 Cypress Semiconductor, 300, 462, 478

D

Daewoo, 362
 Daewoo Securities Co., 168
 Daiei, 295–296
 Daimler, 176
 Daimler-Benz, 153
 DaimlerChrysler, 153, 262, 359, 363, 489, 508
 Dallas Semiconductor Corporation, 344
 Darden Restaurants, 122
 Days Inn, 442
 DB (Deutsche Bank), 487
 Dell Computer, 7, 8, 12–13, 14, 15, 17, 27, 140, 141, 144, 145, 146, 149, 220, 230, 245, 260, 305, 326, 434, 485, 496, 500
 Deloitte & Touche, 90
 Deloitte Consulting, 421

Delphi Corp., 509, 510
 Delta Airlines, 89, 152, 443
 Denny's, 123
 Denso Corp., 509
 Deutsche Bank (DB), 487
 DHL, 229
 Dial, 143
 Dick's Sporting Goods, 202
 Digital Equipment Corporation, 9, 173, 181
 Dillard's Department Stores, 159, 223, 359
 Dineraki, 122
 Dior, 230
 Disney Company, 7, 75–76, 96, 121, 210, 318, 452
 Doc Martin, 144
 Documentum, 464
 DoubleClick, 445
 Doubletree Hotels, 469
 Dow Chemicals, 247259
 DreamWorks SKG, 117–118, 210
 Dresdner Kleinwort Wasserstein, 238
 Du Pont, 17, 125, 223, 225, 272, 388
 DWS, 382

E

Eastman Chemical Co., 439
 Eastman Kodak Co., 118, 242, 279–280, 471
 Eaton Corporation, 408
 eBay, 157, 158, 317–318, 374, 533–534
 E.&J. Gallo Winery, 225
 Electronic Data Systems Corp., 443
 eMachines, 244, 245
 Embraer, 27
 EMC Corporation, 464
 Empire Insurance, 17, 18–19
 Employment Management Association, 123
 ENI, 224
 Enron Corporation, 80, 89, 93, 95, 131, 521–522
 Erie Railroad, 477
 Erlich Transcultural Consultants Inc., 133
 Ernst & Young, 123, 428
 ESPN, 159
 E*Trade, 146, 158
 Exane BNP Paribas, 238

F

Fairchild Semiconductor, 313
 FDA (U.S. Food and Drug Administration), 30–31, 197–198
 Federal Express (FedEx), 228–229, 257, 270
 FedEx (Federal Express), 143, 228–229, 257, 270
 Ferrari, 246
 Financial Times, 499

Finex, 168
 FinnAir, 57
 Fireman's Fund Insurance Co., 464
 FleetBoston Financial Corp., 451–452
 Florida State University, 133
 Foodieland, 84
 Ford Motor Company, 117, 141, 153, 179, 189, 247, 285, 286, 303, 359, 363, 375–376, 388, 431, 489, 503
 Fortune 500 companies, 111, 117, 125, 209, 321–322, 349, 374
 Four Seasons (hotel), 442
 Freddie Mac, 89
 Frito Lay, 218
 Fuji Photo Film Co., 279
 Fujio Cho, 509
 Fulcrum Global Partners LLC, 487

G

G. D. Searle, 140, 226
 E. & J. Gallo Winery, 225
 Gander Mountain, 202
 The Gap, 97, 98, 230, 275
 Gateway, 146, 244–245, 301–302, 307
 Gawker Media, 486
 GE Consumer Finance, 86
 GE Energy, 86, 87
 GE (General Electric), 7, 25, 37–39, 85–87, 96, 163, 203–206, 218, 219, 221, 294, 295, 360, 381, 382, 383, 421, 427, 480, 502, 528–529
 GE Healthcare, 382
 General Electric Capital, 280–281
 General Electric (GE), 7, 25, 37–39, 85–87, 96, 163, 203–206, 218, 219, 221, 294, 295, 360, 381, 382, 383, 421, 427, 480, 502, 528–529
 General Mills, 216, 342
 General Motors Corp. (GM), 17, 123, 141, 153, 198, 225, 237, 267, 286, 310, 363, 375, 431, 447, 465, 489, 510
 Georg-August University, 40, 382
 Georgetown University, 471
 Georgia-Pacific, 369
 German Institute for International & Security Affairs, 39
 Giddings and Lewis Inc., 360
 Gillette, 221, 222, 225, 227, 229, 297
 Glass Ceiling Commission Report, 109
 Glaxo Wellcome, 197, 257
 GlaxoSmithKline (Glaxo), 197–198, 257, 360
 Global Insight, 427
 GM (General Motors Corp.), 17, 123, 141, 153, 198, 225, 237, 267, 286, 310, 363, 375, 431, 447, 465, 489, 510

Goddard Space Flight Center, 183
 Goldman Sachs & Co., 384, 453
 Good Technology Inc., 199
 Google, 217, 453
 Gradient Corporation, 343
 Gucci, 415
 Guzman & Co., 134

H

Hagberg Group, 111
 Hallmark Cards, 262, 389–390, 394, 399, 407
 Hampton Inns, 442
 Harris Interactive Inc., 108, 117
 Hartz Group, 58–59
 Harvard Business School, 198, 435
 Harvard Law School, 485
 Harvard University, 466
 Hawthorne Works, Western Electric Company, 46–47
 H&B (Hillerich & Bradsby), 531–532
 HBO, 159
 Health Newsletter Direct, 444
 Hennes & Mauritz, 230
 Herman Miller, 455–456
 Hershey Foods, 151
 Hewitt Associates, 176
 Hewlett-Packard (HP), 8–9, 17, 23, 56, 57, 79–80, 111, 172, 260, 267, 279, 280, 313, 397, 443, 468, 469
 Hillerich & Bradsby (H&B), 531–532
 Hilton Hotels, 223–224, 469
 Hindustan Lever Ltd., 220
 HispanTelligence, 134
 Hissho Iwai, 345
 Hitachi, 33, 117
 Hoechst, 358
 Hoffman-La Roche Inc., 440
 Home Depot, 3–4, 5, 6, 7, 12, 23, 115, 289–290, 302, 307
 Honda, 154, 224, 272–273, 286, 455
 Honeywell International Inc., 464
 HP (Hewlett-Packard), 8–9, 17, 23, 56, 57, 79–80, 111, 172, 260, 267, 279, 280, 313, 397, 443, 468, 469
 Hubbard & Hubbard, 123
 Humana Inc., 318–319
 Hunter College, 120
 HVB Group, 382
 Hyatt Regency, 442, 469
 Hyundai, 217, 362

I

IBM, 9, 17, 23, 24, 25, 33, 56–57, 78, 79, 118, 140, 141, 146, 149, 150, 161, 173, 226, 260, 267, 305, 361, 426, 429, 469
 IDEO Product Development, 71–73, 76, 78, 404–405, 410
 Igus Inc., 500–501
 ImproveNow.com, 439
 Indians Institute of Technology, 426

Infosys Technologies, 426, 427
 InnSeekers, 122
 Institutional Shareholder Services, 131
 Intel, 6, 73, 140, 144, 149, 207, 217, 360, 416–417, 472, 473
 Isuzu, 153

J

Jacksonville Foods, 402
 Jaeger, 230
 Jaguar, 153
 JCPenney, 223
 JD Power, 495
 Jenny Craig, 124
 Jet Propulsion Laboratory (JPL), 395
 JetBlue Airways, 524–525
 JFK International Airport, 124
 Jiangsu Shagang Group, 169
 Jingle Jim's International Market, 83–85
 J&J (Johnson & Johnson), 107–109, 491
 Jobline International, 428
 John Deere, 19, 311
 Johnson Wax, 396
 Johnsonville Foods, 400
 JPL (Jet Propulsion Laboratory), 395
 Jupiter Research, 487
 JVC, 220, 226

K

KBW Bank Index, Philadelphia, 451
 Kelly Services, 425
 Ketchum Inc., 464
 Kinko's Copies, 228–229
 Kmart, 459, 460, 501
 Kodak, 118, 242, 279–280, 397
 Kraft, 151, 216
 Krispy Kreme, 151
 Kroger Co., 83–84, 84, 134, 384, 494

L

Lambda Legal Defense and Education Fund, 118
 Lands' End, 158, 159, 202, 221
 Latino Health Solutions, 134
 Laura Ashley, 230
 Lazard Freres & Co., 134
 The Learning Company, 210
 LEGO, 247, 259
 Levi Strauss, 141, 159, 222–223
 Lexus, 230, 495
 LG (Lucky Goldstar), 27, 137–138
 Li & Fung, 142–143, 157
 Liberty Travel, 359
 The Limited, 222
 Lincoln Electric, 343, 344
 Lininets Concern, 221
 Lipschultz, Levin, & Gray, 67
 Liz Claiborne, 173
 L.L.Bean, 201–202, 230, 311
 Lockheed Martin, 118, 390–391
 Lotus Development, 397

Louis Vuitton, 415
 Louisville Slugger, 531–532
 Lowe's, 3–4
 Loyola Marymount University, 452
 Lucent Technologies, 9, 10, 30, 118, 241–242, 267, 369, 491
 Lucky Goldstar (LG), 27, 137–138
 Lundberg Family Frames, 148

M

Macromedia, 485
 Macy's, 257
 Maden Technologies, 312–313
 March of Dimes, 6
 MarketResearch.com, 118
 Marsh & McLennan Cos., 129
 Marshall Fields, 263
 Marshall School of Business, University of Southern California, 417
 Mary Kay Cosmetics Inc., 434
 Massachusetts Institute of Technology (MIT), 281
 Matrix Asset Advisors, 87
 Matsushita, 220, 226
 Mattel, 145, 210–211, 275
 Mazda, 153, 503
 McDonald's, 5, 6, 7, 74, 77–78, 98–99, 144, 145, 217, 224, 226, 230, 239, 248–249, 264–264, 433, 474
 McDonald's Hamburger University, 433
 McDonnell Douglas, 352
 McFarlane Companies, 520–521
 McKinsey & Co., 275
 Medtronic, 61
 Meijer, 84
 Merck & Co., 89, 198, 290, 306–307, 479–480
 Mercury Research, 417
 Merrill Lynch, 132, 146, 198
 Mervyn's, 263
 Metabolife, 30–31
 Metro-Goldwyn-Mayer (MGM), 239
 Metropolitan Opera, 39, 381
 MGM (Metro-Goldwyn-Mayer), 239
 Microsoft Corp., 21, 24, 33, 56, 57, 73, 74, 78, 94, 118, 173, 198, 239, 290, 305, 360, 388, 409, 422, 423, 426, 453, 464, 485–486
 Midas Muffler, 303
 Migration Policy Institute, 133
 Miller Beer, 218
 Minority Corporate Counsel Association, 435
 MIT (Massachusetts Institute of Technology), 281
 Mitsubishi, 153
 Monster.com, 428
 Morgan Stanley Financial Services Trust, 451
 Morton Thiokol, 173, 182, 187
 Motorola, 24, 144, 180–181, 421
 MovieLink, 239
 MTV, 159

N

NAACP (National Association for the Advancement of Colored People), 113
 Nanyang Technological University, Singapore, 453
 Napster, 100, 102
 NASA, 173, 182–184, 187, 207, 395, 467, 523–524
 National Association for Female Executives, 124
 National Association for the Advancement of Colored People (NAACP), 113
 National Bank Financial, 199
 National Urban League, 113
 NationsBank Corp., 452
 Natuzzi, 27
 NBC, 143, 203, 218, 239
 Neiman Marcus, 257, 335, 359
 Nestle, 157, 224
 Netscape Communications, 487
 New York University, 108
 Newell Rubbermaid, 262
 Newton (Apple), 178
 NEXT, 26
 Nickelodeon, 366
 Nike, 273, 274, 275, 328–329, 486
 Nikko Citigroup Ltd., 509
 Nintendo, 144
 Nippon Restaurant Enterprise Co., 148
 Nissan, 153
 Nissan Motor Co., 509
 Nokia, 138, 144, 247, 259–260, 382
 Nomura Securities Co., 511
 Northrup Grumman, 390
 NTP Inc., 199
 Nucor, 123, 343, 415–416
 NVE Pharmaceuticals, 30–31

O

O-bento, 147–148
 OFCCP (Office of Federal Contract Compliance Program), 352
 Office of Federal Contract Compliance Program (OFCCP), 352
 Ogilvy & Mather, 361
 Ohio State University, 363
 The Olive Garden, 433
 Opel, 153
 Orace, 307
 Oracle, 21, 140, 283–284, 286, 298

P

Packard Bell, 9
 PAETEC Communications, 51–52, 59, 65
 Palm One, 8–9, 72, 259
 PalmSource Inc., 198
 Panasonic, 220, 226
 Patagonia, 530–531
 Paul, Hastings, Janofsky & Walker LLP, 352

PepsiCo, 141, 151, 154, 218, 226, 228, 230, 232
 Perdue Farms, 388
 Perimeter Institute for Theoretical Physics, 199
 Pefkins Cole LLP, 352
 Peugeot, 237, 238
 P&G (Procter & Gamble), 52, 134, 141, 143, 218, 221, 228, 311
 Philadelphia KBW Bank Index, 451
 Philip Morris, 218
 Philips NV, 204–205
 Phillips NV, 137
 Pier I Imports, 222, 253
 Pike Place Fish, 529–530
 Pinxav, 63
 Pixar, 26, 210
 Plexus Corp., 268–269
 Polo, 222
 Posco, 168–169
 Prada, 415
 PriceWaterhouseCoopers, 57, 90, 397
 Princeton University, 67
 Procter & Gamble (P&G), 52, 134, 141, 143, 218, 221, 228, 311
 Putnam Investments, 62

Q

Quaker Oats, 151
 Quaker State Corp., 471
 Quantum, 140

R

Radio Shack, 159, 225, 326
 Rainbow Coalition, 114
 Ralph Lauren, 220
 Rational Software, 57
 Raytheon, 118
 RE/MAX International Inc., 344
 Red Lobster, 433
 Reebok, 274
 Regency Centers Corp., 84
 Reliant Stadium, Houston, 39
 Renault, 153, 238
 Reputation Institute, New York University, 108
 Research in Motion Ltd. (RIM), 198–199
 Retail Forward Inc., 384
 RIM (Research in Motion Ltd.), 198–199
 Risk International Services, 388
 Road Runner, 487
 Robert Bosch, 509, 510
 Rochester Institute of Technology, 280
 Rock Bottom Restaurants Inc., 393
 Rolex, 220
 Rolls Royce, 246, 473
 Ronald McDonald House, 387
 Royal Dutch Shell, 208–209

S

S. C. Johnson & Son, Inc., 118
 Saab, 153

Safeway, 384
 Samsung, 27, 137, 138, 362
 SAP, 21, 144, 145
 SAS Institute, 321–322, 323
 Schering and Hoechst, 27
 Scott & White Healthcare System, 382
 Seagate Technologies, 140
 Sears, 219, 223, 501
 SEC (U.S. Securities and Exchange Commission), 62, 96, 129
 Security Pacific Corp., 452
 Seiyu Ltd., 510–512
 Selig Center for Economic Growth, University of Georgia, 132
 Semco, 419–420, 437, 439
 7-11 Stores, 216
 Shanghai BaoSteel Group, 169
 Shell, 208–209
 SICO (Starr International Co.), 130
 Siegel Management Consultants, 172
 Siemens, 39–40, 371–372, 373, 381–383
 Simon & Schuster, 256, 470
 SiteDesign, 345
 siteROCK, 302
 SmithKline Beechum, 197, 257
 Social Security Administration, 132–133
 Sony, 138, 144, 220, 238–239, 275, 499–500
 Southern California Edison, 118
 Southwest Airlines, 52, 106, 267, 387–388, 405, 408, 492, 493, 494
 Spider Man, 238–239
 Sprint, 427
 Stamford (Connecticut) Symphony Orchestra, 368
 Standard & Poor's (S&P), 129
 Stanford University, 176
 Starbucks, 532–533
 Starr Foundation, 130
 Starr International Co. (SICO), 130
 Steelcase, 455
 Stetson University, FL, 383
 Storability Software, 426
 Stringer, Howard, 239
 Subway, 216, 249
 Sun Microsystems, 73, 179–181, 182, 184, 199, 485
 Sunflower Electric Power Corporation, 307

T

Tacit Knowledge Systems Inc., 390–391
 Taqueria Arandas, 122
 Target, 121, 142, 159, 219, 263, 275, 303, 326, 383
 Target Corp., 452
 TD Waterhouse, 146
 TelePort Corporation, 469
 Telia, 428
 Texas A&M University, 75

Texas Instruments (TI), 313
 Three Mile Island nuclear plant, PA, 458
 3M, 25, 37–39, 191–192, 305
 TI (Texas Instruments), 313
 TIAA-CREF, 123
 Time Warner Inc., 176, 239, 336–337, 486–487
 TNS Media Intelligence/CMR, 135
 Tokio Marine and Fire Insurance, 345
 Tommy Hilfiger, 220
 TopCoder Inc., 453
 Toshiba, 239
 Tower Automotive, Inc., 375–376
 Toyota Motor Corp., 114, 117, 154, 224, 229–230, 272–273, 281, 286, 288, 363–364, 489–490, 494, 495, 504, 508–510
 Toys 'R' Us, 143–144, 221
 Travel Company, 359
 Tungsram, 163–164
 TWA, 124
 Tyco, 80, 93

U

Unilever, 143, 156–157, 220
 Union Bank of California, 31–32
 United Airlines, 118, 152, 239
 United Auto Workers Union, 447
 United Electric Controls, 501–502
 United Food & Commercial Workers Union, 384
 United Parcel Service (UPS), 118, 143, 228–229, 270, 304–305, 307–308, 362, 468
 United Workers Union, 117
 UnitedHealth Group, 319
 Universitas Katolik Parahyangan, Indonesia, 453
 University of California - Los Angeles, 118
 University of Georgia, 132
 University of Houston, 115
 University of Michigan, 197, 435
 University of Notre Dame, 115
 University of Southern California, 417
 University of Wurzburg, 382
 Univision Communications Inc., 133, 135
 UPS (United Parcel Service), 118, 143, 228–229, 270, 304–305, 307–308, 362, 468
 U.S. Census Bureau, 110, 112, 113, 116, 133
 U.S. Department of Labor, 132, 352
 U.S. Food and Drug Administration (FDA), 30–31, 197–198
 U.S. Internal Revenue Service (IRS) DP, 132
 U.S. Justice Department, 129
 U.S. Postal Service (USPS), 143, 228

U.S. Securities and Exchange
Commission (SEC),
62, 96, 129
U.S. Supreme Court, 93
USPS (U.S. Postal Service),
143, 228

V

Vandercar Holdings
Inc., 84
VeriFone, 397
Verizon, 138
VF Corp, 222
Viacom, 239, 255–256
Visa International, 427

Volkswagen, 25, 237–238, 510
Volvo, 153

W

Wal-Mart Stores, Inc., 6, 76–77,
83–85, 141, 143, 146, 159,
189, 190, 212, 219, 223,
226, 230, 275, 295–296,
307, 326, 383, 384, 459,
460, 501, 510–512
Walmart.com, 459, 460
Walt Disney Company, 7, 75–76,
96, 121, 210, 318, 452
Warner Brothers, 210, 239
Waterford, 227
Web Industries, 388
Wells Fargo & Co., 452
Western Electric Company,
46–47
Westinghouse, 272
Whirlpool, 397, 421
Whole Foods, 355–356, 357
Wild Oats, 519
Witeck Communications Inc., 117
World Trade Organization
(WTO), 156
WorldCom, 80, 93
WTO (World Trade
Organization), 156
Wuhan Iron & Steel Group, 169
Wyatt Co., 65
Wyoming Business Council, 63

X

Xerox, 280–281, 289, 311

Y

Yahoo!, 145, 147, 486
Yokohama Tire Corp., 471

Z

Zara, 230–231
Ziff-Davis, 486

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